The Southland Corporation

1987 Corporate Profile

And Form 10-K Annual Report for the Year Ended December 31, 1987

The Southland Corporation

The Southland Corporation, which originated the convenience store concept in 1927, is the largest convenience store chain in the world and one of the United States' largest independent gasoline retailers.

At the end of 1987, Southland operated 7,818 7-Eleven stores and 432 other convenience stores in the United States and Canada. Area licensees and affiliates operated another 4,614 stores in 14 foreign countries, Puerto Rico, Guam and certain parts of the United States.

Sales from all convenience stores, which comprise the largest portion of the Company's revenues, exceeded $8 billion in 1987. This figure does not include sales from the stores operated by affiliates and area licensees.

The convenience stores are supported by five regional distribution centers and six food centers, strategically located across the United States.

Southland also owns a 50-percent equity interest in Citgo Petroleum Corporation, the country's largest independent refiner/marketer. In addition to a refinery at Lake Charles, Louisiana, one of the country's largest, and a lubricants compounding/packaging plant, Citgo has varying ownership interests in a lubricants refinery, 42 refined product terminals and more than 15,500 miles of pipelines.

Southland and 7-Eleven have always practiced good corporate citizenship, due in large part to management's belief that it makes good business sense to support the needs of the communities in which the Company operates. Individual 7-Eleven divisions use their stores' high neighborhood visibility to participate in a wide range of local projects. Employees, franchisees, customers and suppliers have raised more than $53 million for the Muscular Dystrophy Association since 1976, more than any other corporate sponsor of the Jerry Lewis Labor Day Telethon. In addition, Southland sponsors the 7-Eleven Cycling Team, the premier American bicycling team that is also rapidly becoming an important force in European racing events.

About the Cover: More than seven million customers shop at their neighborhood 7-Eleven stores every day.

From the Chairman and President and Chief Executive Officer

Southland has prospered for 61 years as the convenience store industry leader for many reasons, but perhaps most notably because of its ability to innovate and adapt to change. These same qualities enabled the Company in 1987 to complete one of the largest leveraged buyouts (LBO) in history during the most tumultuous financial period in recent memory.

We are confident that the future of convenience retailing is very bright. We are also confident of Southland's place in the industry's future, because we believe we have an unbeatable combination of the most experienced management, skilled and knowledgeable employees and franchisees, and superior store sites.

When the LBO was announced last July, we stated our intention to focus on our core 7-Eleven convenience retailing business for the future. 7-Eleven will continue to receive important support from Southland's five regional distribution centers and six food centers, which also contribute earnings from outside customers. The other major component of the "new" Southland is our 50-percent interest in Citgo Petroleum Corporation, which provides us with a long-term competitively priced supply of branded gasoline.

Proceeds from the sale in 1986 of a half-interest in Citgo to a subsidiary of Venezuela's state-owned oil company, Petroleos de Venezuela, S.A. (PDVSA), significantly reduced our investment in Citgo. Through its own subsequent refinancings, Citgo has repaid its loans to both parent companies. Furthermore, in February 1988 Citgo paid its first cash dividend, $12.5 million each to Southland and PDVSA, a good indicator of Citgo's strengthened financial position.

To help repay a portion of the nearly $4 billion of debt incurred in the LBO, we announced we would sell our Dairies Group, Chief Auto Parts, Tidel Systems, Reddy Ice, the Snack Foods division and the Chemical/Food Labs division, as well as about 1,000 convenience stores, or 12 percent of our store base. Because these divestitures and a monetization of the yen royalties from our licensee in Japan are ahead of schedule, we will be able to repay a portion of our debt early and thereby reduce our interest costs substantially. As we hoped, the businesses to be divested are being sold as ongoing operations. This is very gratifying since it preserves the greatest number of jobs for our former employees.

After the divestitures, we will still operate more than 7,000 stores in markets that offer us the greatest growth potential. We intend to focus our outstanding management and marketing resources on maximizing the sales and profitability of our existing store base. And that store base is *extremely* impressive and well-positioned in the most attractive markets in the United States. We have invested heavily in these stores over the last three years — for remodeling, new construction and important new marketing programs such as fast foods and self-serve beverage bars. About 70 percent of these stores are located on high-visibility corners, and 37 percent offer self-serve gasoline, which produces many incremental merchandise purchases as well as substantial gross profits.

We have moved quickly to implement new operating strategies. Among the most important of these strategies has been the reorganization of our Company to achieve greater cost-efficiency and to place decision-making authority as close to the store level as possible, making the entire Company even more responsive to our customers' needs. These and other changes have played a major role in helping us achieve our new financial objectives, including our expense reduction targets.

With the LBO and 7-Eleven reorganization behind us, and as we near the end of our divestiture program, we're quite pleased to return our full attention to our core convenience retailing business, including our distribution and food centers. We deeply appreciate the outstanding efforts and support of our employees, franchisees and suppliers, and have asked them to join us in rededicating ourselves to our #1 priority — offering our customers the best possible service and value.

John P. Thompson

John P. Thompson
Chairman of the Board

Jere W. Thompson

Jere W. Thompson
President and
Chief Executive Officer

April 5, 1988

7-Eleven Shows Strong Gross Profit Increase for 1987

At the end of 1987, Southland operated 7,818 7-Eleven stores, 319 High's Dairy Stores and 113 Quik Mart and Super-7 high-volume gasoline locations, in 41 states, the District of Columbia and Canada. After completing the planned sale of about 1,000 stores in selected markets, the Company will operate more than 7,000 convenience stores in 34 states, D.C. and Canada. 7-Eleven will continue to benefit from the geographical diversity of its store base, which helps protect it from regional economic downturns.

Sales from all stores totaled $8.04 billion in 1987, a gain of 8.8 percent over the previous year. Merchandise sales and gross profit increased 9.6 and 9.7 percent, respectively, in 1987, as 7-Eleven benefited from substantial past investment in programs such as fast foods and self-serve beverage bars. Gasoline gross profit decreased 8.9 percent, however, primarily due to a 6.4 percent drop in average gross profit per gallon. In addition, gasoline volume declined 2.6 percent in 1987 to just under two billion gallons, largely because of the net reduction of 45 high-volume gasoline units.

High-quality fast foods, such as freshly made deli-style sandwiches, hot dogs and nachos, are an important part of 7-Eleven's marketing strategy.

The healthy increase in merchandise gross profit offset the decline in gasoline gross profit to produce an 8.0 percent increase in total gross profit. The sales and gross profit increases for 1987 include stores that the Company intends to divest in 1988, which generally have lower average margins than the stores to be retained.

Operating profits for the stores were reduced by higher occupancy costs resulting from extensive store remodeling and start-up costs associated with marketing programs, most notably in the first half of the year. During that time 7-Eleven was introducing or expanding fast food programs and customer services at an unprecedented pace.

7-Eleven Has Best Name Recognition, Store Base in Industry

7-Eleven's success in recent years has resulted largely from three key factors — its extremely valuable name recognition, the breadth and quality of its store base, and the effective, innovative marketing of its products and services. And today, more than ever, these elements are critically important to our continuing leadership in convenience retailing.

7-Eleven not only leads its own industry in name recognition and store base, but it ranks extremely high among *all* retailers for these factors.

The name "7-Eleven" has been used continuously by Southland since 1946, and it is literally synonymous with "convenience retailing" across the country. More than seven million customers shop at their neighborhood 7-Eleven stores every day.

The exceptional value of the "7-Eleven" name can be quantified by the interest shown in franchising and licensing of 7-Eleven stores. 7-Eleven was named one of the United States' top ten franchises in a 1987 survey by Entrepreneur magazine, and individual franchisees operated 39 percent of the 7-Eleven stores open at the end of the year. Internationally, area licenses for 7-Eleven stores have been granted to companies in five foreign countries, Puerto Rico and Guam/Micronesia in the last two years alone.

Approximately 70 percent of all 7-Eleven stores are located on corner sites, more stores than there are in the entire store base of the industry's next largest chain. Corner locations are particularly valuable in the convenience retailing business, because they provide increased visibility and access to passing traffic, as well as more convenience for customers.

Fast Foods, Services Differentiate 7-Eleven from Competition

Over the past several years, changing demographics and lifestyle patterns have increased the demand for convenience. 7-Eleven has adapted to these trends, as it has for six decades of changing American lifestyles.

7-Eleven stores offer a full line of up to 3,000 products and services, including gasoline in many cases, at stores that are generally open around the clock. In recent years, 7-Eleven has aggressively differentiated itself from the mini-convenience "g-stores" operated by the major oil companies.

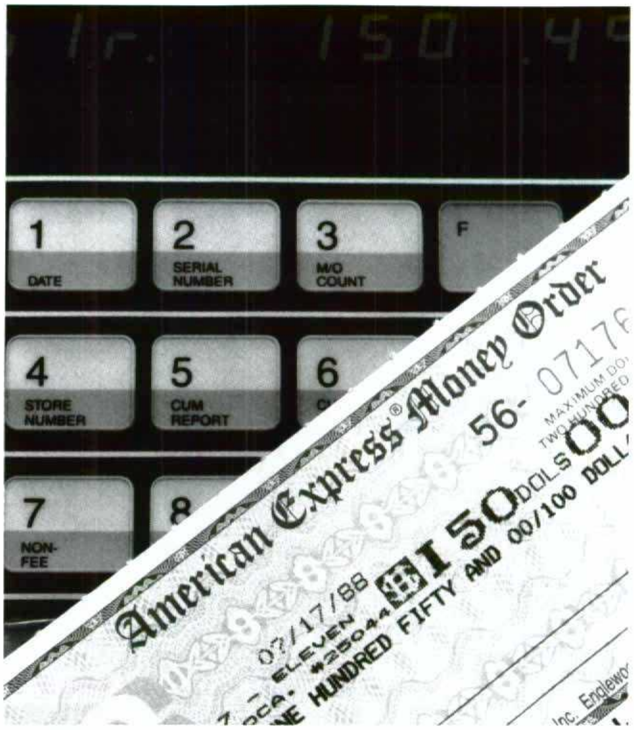
The difference between 7-Eleven and many of its competitors is that 7-Eleven stores continue to provide a full range of everyday "fill-in" products, in addition to videocassette rentals, automatic teller machines, electronic money order machines, and delicious fresh-made deli-style sandwiches and bakery products — and all at very competitive prices. This one-stop "value package" has proven popular with both old and new 7-Eleven customers.

7-Eleven's involvement with high-quality fast foods and electronic services has been well-established for several years now.

For example, the following table indicates what percentage of 7-Eleven and the total population of traditional convenience stores and "g-stores" offered three of the most popular marketing programs in convenience retailing at the end of 1986, the last date for which industry numbers are available. The depth of 7-Eleven's market saturation for these programs, which has since increased further, is the result of Southland's sizeable investment over the last few years. Together with the high quality of its store base, 7-Eleven's new product/service breadth demonstrates why its stores will be able to maintain a very strong competitive position at reduced capital spending levels over the next few years.

	7-Eleven*	All Conventional Convenience Stores**	All "G-Stores"**
Hot Dogs	83%	48%	65%
Movie Rentals	56%	28%	20%
Money Orders	70%	49%	45%

Sources: **7-Eleven product/service depth as of 12/31/86*
***The Convenience Store News, May 29, 1987, "Industry Report" for 1986*



Buying a money order at 7-Eleven is faster and easier than ever before, due to new timesaving electronic machines.

7-Eleven continued to add high-quality fast foods during 1987. Fresh-made deli-style sandwiches are now being prepared on-premises at 57 percent of the stores, complemented by self-serve condiment bars at many locations, and 85 percent of the stores currently offer hot dogs and nachos. A variety of hamburgers, other hot sandwiches and pastries are sold at 37 percent of the locations. Soup-to-go and pizza are also available at selected stores. 7-Eleven's large variety of fast foods, including literally everything from "soup to nuts," offers customers a wider choice for a quick meal than is available at most fast food restaurants. Agreements with nationally known suppliers for various items, such as doughnuts, will expand in-store display opportunities, improve quality and offer greater value to 7-Eleven customers.

7-Eleven's customer services, including automatic teller machines (ATMs), electronic money order sales and videocassette rentals, also differentiate it from many of its competitors. These services maximize the value of "one-stop shopping," thereby attracting more people into the store and increasing incremental merchandise and gasoline sales.

7-Eleven's "MovieQuik" videocassette rental program offers a well-stocked supply of the most popular movie titles, competitive prices and around-the-clock convenience.

ATMS, now available at approximately one-fourth of the stores, attract customers because they accept a wide variety of bank cards and are accessible 24 hours a day. Research indicates that 58 percent of 7-Eleven ATM customers purchase gasoline or merchandise with their newly dispensed cash.

7-Eleven has been selling money orders for more than 30 years and has long been second only to the United States Postal Service in money order sales. In order to maximize the sales potential of this service, management decided in 1985 to begin upgrading the processing capability of 7-Eleven's equipment. As a result, new electronic money order machines are currently operating in almost 85 percent of the stores. These machines, with their enhanced security and timesaving features, have enabled 7-Eleven to substantially increase money order sales volume.

"MovieQuik," Southland's videocassette rental program, offers exciting traffic-building and cross merchandising potential. It also addresses a market niche not covered by traditional video retailers, with almost 6,500 easily accessible locations that never close. Regular rotation of each store's 200-tape selection, including the most frequently requested movie titles, encourages repeat rentals.

7-Eleven's involvement in the videocassette rental market is well-justified by the enormous customer base, as well as its commitment to offer convenient, one-stop shopping. Sixty percent of all American households own videocassette recorders, and more than 80 percent are expected to own them by 1990. More than half of all "MovieQuik" customers buy other 7-Eleven merchandise, and they tend to have higher household incomes than the typical 7-Eleven customer. As an added benefit, each rental involves *two* trips to the store, and one of the two peak rental periods occurs during winter months, historically 7-Eleven's slowest season.

Lottery ticket sales are popular in 7-Eleven stores in 21 states and the District of Columbia. In addition to providing another source of revenues and gross profits, lottery tickets help build customer traffic that can lead to other merchandise sales. Florida successfully introduced a statewide lottery in early 1988, and a strong promotional campaign by 7-Eleven helped produce record first-week sales for the state.

7-Eleven is aggressively exploring other services that can be implemented with little or no capital investment by Southland.

1987 Convenience Store Sales by Category

Gasoline	22.7%
Tobacco	16.3
Beer/Wine	11.2
Soft Drinks	10.7
Food Service	8.4
Groceries	8.3
Non-Foods	6.1
Dairy Products	5.1
Candy	3.7
Baked Goods	3.3
Health/Beauty Aids	2.4
Customer Services	1.8
Total	100.0%

The Company does not record sales by product lines, but estimates the percentage of 7-Eleven sales by principal product category based upon total store purchases.

Core Products, "Slurpee" and Gasoline Still Going Strong

7-Eleven is also working closely with its vendors to enhance all marketing aspects of its core products, such as coffee, soft drinks, beer, cigarettes, candy and chips. Eye-catching in-store merchandising displays and creative "cross-promotion" ideas are expected to increase sales in these product categories.

"Slurpee," 7-Eleven's frozen carbonated beverage that is famous for its appeal to all ages, will receive a new taste in 1988. Southland has signed an agreement with Coca-Cola USA to use Coca-Cola classic, Sprite, Minute Maid orange and Fanta syrup flavors for "Slurpees" in 7-Eleven stores across the nation. More than three billion "Slurpees" have been sold since its introduction in 1965, a performance record that will be further enhanced by the union of two of the country's best-known brand names.

Self-serve gasoline, which has accounted for approximately one-fourth of total 7-Eleven sales since 1980, is a major part of the Company's overall marketing program. Southland steadily increased gallonage from 1980 through 1986, expanding its market share while total U.S. consumption remained relatively flat. Gasoline sales contribute substantial gross profits without requiring additional labor. It is also an important in-store traffic builder, since 40 percent of all gasoline customers buy merchandise.

7-Eleven is one of the few retailers that allows customers to pay for gasoline and merchandise purchases with checks, and a majority of the stores also accept bank cards. Self-serve gasoline is available at about 37 percent of Southland's convenience stores, with the majority offering Citgo-branded gasoline. These stores offer the added payment convenience of the "Citgo Plus" credit card, which has an active cardholder base of 825,000 customers.

International Expansion, Distribution and Food Centers Contribute to 7-Eleven Success

Southland's International division offers exciting opportunities for continued expansion of the 7-Eleven name. New area licenses were granted for 7-Eleven stores in Spain, Indonesia and Puerto Rico during 1987. At year-end, the division was coordinating the activities of 4,093 7-Eleven stores operated primarily by licensees in 14 foreign countries, Puerto Rico and Guam, as well as 521 stores operated by licensees in the United States. Sales from these stores are not included in Southland's revenues.

7-Eleven's International Presence*

Japan	3,245 stores
Hong Kong	210
Taiwan	168
Singapore	63
Malaysia	54
Australia	121
United Kingdom	49
Norway	13
Philippines	8
Republic of Ireland	2
Panama	2
Guam/Micronesia	1
Puerto Rico	1
Spain	1
Sweden**	65
Mexico**	90
	4,093 stores

*As of Dec. 31, 1987
**Stores operated by affiliates. Stores in all other countries operated by area licensees.

In 14 foreign countries, Guam and Puerto Rico, 7-Eleven translates as "convenience" in more than 4,000 stores operated by international licensees and affiliates.

Five highly automated distribution centers serve 75 percent of the 7-Eleven stores, as well as outside convenience retailing and food service customers.

Southland's five distribution centers and six food centers supply over 9,600 retail and food service customers in 43 states, the District of Columbia and Puerto Rico, including 75 percent of the Company's convenience stores. Computerized ordering and route scheduling and the ability to supply products in small quantities make the distribution system one of the most efficient in retailing. The centers enable 7-Eleven and other customers to manage their inventories more effectively, maintain fresher merchandise, and generate higher sales and profits in limited selling space. Total 1987 sales of $1.57 billion included outside sales of $352.6 million, and profits increased 5.0 percent over 1986.

Citgo Reports Excellent 1987 Results

1987 was Citgo Petroleum Corporation's first full year under joint ownership by Southland and Petroleos de Venezuela, S.A., (PDVSA). Southland's $53 million equity in Citgo's net earnings for the year largely reflected the stabilizing impact on Citgo's operations of its 20-year crude oil supply agreement with PDVSA. In addition, Citgo continued to benefit from its ongoing cost control and aggressive branded gasoline marketing programs, as well as its profitable lubricants, pipeline and industrial products businesses.

Crude runs at Citgo's Lake Charles, Louisiana, refinery averaged 241,000 barrels per day. A record 59 percent of that feedstock mix was heavy sour crude oil, resulting chiefly from the supply agreement with PDVSA. Because of its feedstock upgrading capability, the refinery's gasoline yield per barrel of crude oil processed was about 70 percent, further benefiting Citgo's light fuels margins.

Citgo continued to expand and improve its branded distribution and marketing network during 1987. In addition to more than 2,000 7-Eleven stores carrying Citgo-branded gasoline, Citgo supplies about 4,800 other retail gasoline outlets through 337 branded distributors. Over 70 percent of its branded gasoline requirement is met by Citgo's refinery production. Citgo's 92-octane gasoline, "The Performer," accounted for 42 percent of the refinery's total gasoline production, largely due to construction of a methyl tertiary butyl ether (MTBE) unit that began operation in August. This unit increased by 15 percent the refinery's capability to produce high-quality premium unleaded gasoline, enabling Citgo to better respond to increasing consumer demand for that product.

Citgo also increased its refined product storage capacity by expanding tankage at existing terminals and acquiring interests in additional sites. Citgo's varying ownership interests in these terminals and over 15,500 miles of crude oil and refined product pipelines provide a stable income source.

Citgo exceeded last year's sales volumes of finished lubricants and refined waxes, despite a continuing decline in industry demand. Citgo's commitment to this business was reflected in the addition of a $17 million "process computer control" project, brought online during 1987 to further improve operating efficiency at its jointly owned Cit-Con lubricants and wax refinery.

The industrial products business unit provided a significant contribution to Citgo's earnings in 1987, reflecting strong domestic and international demand for polymer-grade propylene, as a result of continuing prosperity in the petrochemical industry.

Self-serve gasoline is available at 37 percent of Southland's convenience stores, with a majority offering Citgo-branded product. Gasoline increases customer traffic and gross profit without additional labor.

Southland's New Operating Strategies, Financial Objectives

As soon as the LBO of Southland was announced on July 5, 1987, the Company began reshaping its organizational structure and operating strategies to reflect a new set of corporate objectives. These include increased emphasis on cash flow, as well as earnings before interest, tax, depreciation and amortization (EBITDA). Management compensation is now tied closely to maximization of existing stores' profitability, as opposed to growth in number of units. Construction of new stores will be curtailed for the immediate future, due to the need to use cash from operations to repay the LBO debt and the resulting reduction in available capital funds.

Due to the size, quality and condition of its existing store base, the Company does not feel that this period of restricted capital investment poses a threat to 7-Eleven's leadership position in the convenience retailing industry. Furthermore, Southland has sufficient capital funds available to maintain the excellent condition of its stores.

Accounting Changes, Higher Interest Payments and Noncash Expenses Affect Reported Results

Because of the LBO, generally accepted accounting principles (GAAP) required Southland to revalue its assets in accordance with purchase accounting as of August 1. Southland in fact reported financial results for the year in two periods. Results from January 1 through July 31, the period preceding completion of the LBO-related tender offer, were recorded based on the Company's historical cost accounting basis. Purchase accounting was used to revalue two-thirds of the Company's net assets for the period from August 1 through December 31, the period during which at least two-thirds of Southland's outstanding common stock was owned by JT Acquisition Corporation, an affiliate of the founding Thompson family's private investment firm. The remaining one-third of net assets was revalued as of December 31, 1987, after the merger of Southland and JT Acquisition was completed.

The revaluation of the Company's property, plant and equipment resulted in a "fair value" that was substantially higher than their former book value, leading to sharply increased depreciation expense during the last five months of 1987. Depreciation expense will continue at a high level in the future.

In addition, the Company incurred a much higher level of noncash amortization expense as of August 1. This included amortization of the excess of the purchase price over the "fair value" of the assets that was paid by JT Acquisition Corporation, as well as amortization of other intangible assets. The Company also began to record the debt and related interest expense used to finance the LBO, along with certain other nonrecurring fees and expenses.

For all of these reasons, the following results from the two periods are not comparable and cannot be added to achieve 1987 full-year financial results. For the seven months ended July 31, under historical cost accounting, total revenues for continuing operations and the convenience stores to be divested were $4.90 billion. Net earnings for the seven months were $90.1 million. For the five months ended December 31, reflecting purchase accounting for two-thirds of the Company's net assets, total revenues for continuing operations only were $3.2 billion, and a net loss of $149.7 million was recorded.

Because of the increase in interest payments on the large amount of debt incurred in the LBO, as well as high noncash expenses such as depreciation and amortization, Southland does not expect to report a net profit for several years. Nevertheless, management intends to maintain contributions to The Southland Corporation's Employees' Savings and Profit Sharing Plan as long as the Company continues to perform well at the operating level.

Southland's Capitalization After the LBO

The Company's capitalization following the LBO consists of approximately $2.5 billion in bank loans, $1.5 billion in publicly held high-yield bonds, $247 million stated value of a new class of publicly held preferred stock, debt existing prior to the LBO of approximately $589 million, of which $201 million were capital lease obligations, and a revolving bank credit facility.

The revolving credit facility is used to meet the Company's short-term operating requirements and cannot exceed $450 million at any one time. Availability is reduced for any letters of credit issued under this facility. The amount borrowed under the facility fluctuates through the year, due to the strong seasonality of the Company's business. Because convenience store sales are substantially lower in the winter than in the rest of the year, borrowings against the revolving credit facility are heaviest during those months. However, as of December 31, 1987, only $25 million was outstanding under this facility, due to the sharp curtailment of capital expenditures.

Southland has placed interest rate caps or swaps on about $1 billion of its floating rate bank debt. The balance of the bank debt is subject to floating interest rates, either the prime rate plus 1.5 percent or the London interbank offered rate plus 2.5 percent.

Repayment of LBO Debt Progresses Well

The Company plans to repay approximately $1 billion of its bank loans through divestitures of food processing and manufacturing operations, Chief Auto Parts and about 1,000 convenience stores, as well as the monetization of royalty payments from its 7-Eleven licensee in Japan. As of April 5, Southland had completed the sale of its Dairies Group, Tidel Systems and MovieQuik divisions, as well as 754 operating stores and related real estate. The Company had also executed a financing agreement at a favorable interest rate with a syndicate of Japanese institutions for 41 billion yen or approximately $325 million (based on 126 yen per $1), collateralized by the Japanese royalties. Principal and interest on the loan are nonrecourse to Southland. The Company also expects to close by mid-1988 on the pending sales that have already been announced, which include 21 convenience stores, Chief Auto Parts and Reddy Ice. Overall, net proceeds should be well within the range projected before the LBO. In addition, the store divestitures and yen monetization will be completed a year ahead of schedule, resulting in substantial interest savings.

By the end of 1987, Citgo Petroleum Corporation had completely repaid its loans to both Southland and Petroleos de Venezuela, S.A. (PDVSA). Proceeds from Citgo's repayment of $100 million to Southland were used to reduce the level of borrowing for the second and final merger stage of the LBO. Also, Southland received its first cash dividend from Citgo, $12.5 million, in early 1988.

More detailed information about the Company's financial position, including its bank credit agreement, publicly issued debt securities and preferred stock, and 1987 financial results, may be found in the Form 10-K for the year ended December 31, 1987.

Corporate and Financial Information

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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934.

For the Fiscal Year Ended December 31, 1987 **Commission File Number 0-676**

THE SOUTHLAND CORPORATION

(Exact name of registrant as specified in its charter)

Texas (State or other jurisdiction of incorporation or organization)	**75-1085131** (I.R.S. Employer Identification No.)
2828 North Haskell Ave., Dallas, Texas (Address of principal executive offices)	**75204** (Zip code)

Registrant's telephone number, including area code, 214-828-7011

Securities Registered Pursuant to Section 12(g) of the Act:

15% Cumulative Exchangeable Preferred Stock, Series One

15¾% Senior Subordinated Notes due 1997
16½% Senior Subordinated Discount Notes due 1997
16¾% Subordinated Debentures due 2002

Units consisting of
18% Junior Subordinated Discount Debentures due 2007 and
26,135,682 Warrants
(Title of class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ✓ No ___ .

The aggregate market value of the voting stock held by non-affiliates of the registrant was $-0- at March 28, 1988. (All Common Stock, $.01 par value, the only class of voting stock of the registrant, is held by affiliates of The Thompson Company, see Part III, Item 12, Security Ownership of Certain Beneficial Owners and Management.)

200,000,000 shares of Common Stock, $.01 par value (the registrant's only class of Common Stock), were outstanding as of March 28, 1988.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the following documents are incorporated by reference into the listed Parts and Items of Form 10-K:

None

PART I

Item 1. *BUSINESS.*

The Company

The Southland Corporation is one of the leading specialty retailers in the United States and is the country's largest operator and franchisor of convenience stores, doing business principally under the name 7-Eleven®. During 1987 Southland was also a major processor of dairy products which were distributed under 10 regional brand names. At December 31, 1987, the Company's operations included 7,818 7-Eleven convenience stores in the United States and Canada, 319 High's Dairy Stores, 469 Chief® Auto Parts stores, five distribution centers, six food processing centers, 113 Quik Mart® and Super-7® high volume gasoline outlets with mini-convenience stores, manufacturing and distribution of specialty chemicals, ice, chips, snack foods and safe-like devices and monitoring devices for underground storage tanks and the refining, marketing, transportation and distribution of petroleum products through its 50-percent owned subsidiary, Citgo Petroleum Corporation ("Citgo"). The Company also (a) owns Svenska/7-Eleven AB, which, at December 31, 1987, operated 65 stores in Sweden, and (b) had an equity interest in 90 Super Siete stores in Mexico at year end. Area licensees, or their franchisees, operate additional 7-Eleven stores in certain areas of the United States, and in Australia, Guam/Micronesia, Hong Kong, The Republic of Ireland, Japan, Malaysia, Norway, Panama, the Philippines, Singapore, Taiwan and the United Kingdom. Area licenses were granted during 1987 covering Indonesia, Puerto Rico and Spain.

At a special meeting of shareholders, originally scheduled for November 5, 1987, and adjourned to December 8, 1987, the shareholders of the Company approved an Agreement and Plan of Merger (the "Merger Agreement"), dated as of July 3, 1987, as amended, between the Company and JT Acquisition Corporation ("JT Acquisition"), a Texas corporation formed at the direction of The Thompson Company, a Texas corporation and an affiliate of Messrs. John P. Thompson, Jere W. Thompson and Joe C. Thompson, Jr. (the "Thompsons"). Pursuant to the Merger Agreement, JT Acquisition was merged (the "Merger") with and into the Company, with the Company as the surviving corporation. John P. Thompson is the Chairman of the Board and a director of the Company, Jere W. Thompson is the President and Chief Executive Officer and a director of the Company and Joe C. Thompson, Jr. is a director of the Company. The Merger, which occurred on December 15, 1987, was the second step in the acquisition of the Company by the shareholders of JT Acquisition, the first step of which was a cash tender offer for 31,500,000 (approximately 64 percent of the outstanding) shares of the Company's common stock and all outstanding shares of the Company's $4.00 Cumulative Convertible Exchangeable Preferred Stock, Series A (the "Tender").

To finance the Tender and Merger, JT Acquisition entered into a Credit Agreement, dated as of July 31, 1987 (the "Credit Agreement"), with Citicorp Industrial Credit, Inc. ("Citicorp"), Bankers Trust Company, Bankers Trust (Delaware), Manufacturers Hanover Trust Company, Security Pacific National Bank, and Canadian Imperial Bank of Commerce, who serve as agents under the Credit Agreement, and certain financial institutions (the "Banks") providing for, among other things, the making of loans and advances in an aggregate amount not to exceed $3 billion.

At the time of the Merger, the Company obtained permanent financing, which consisted of (i) $2 billion of term loans from the Banks (the "Senior Term Loans"), (ii) $495 million of term loans from the Banks to be repaid with a portion of the proceeds from the Divestitures (as defined below) and from other sources (the "Divestiture Term Loans"), (iii) $450 million of revolving credit loans from the Banks (the "Revolving Credit Facility"), (iv) the proceeds of the sale of $350,000,000 15¾% Senior Subordinated Notes due 1997; $402,260,000 16½% Senior Subordinated Discount Notes due 1997; $500,000,000 16¾% Subordinated Debentures due 2002; and 946,945 Units consisting of $946,945,000 18% Junior Subordinated Discount Debentures due 2007 and 26,135,682 Warrants and (v) the issuance of the 15% Cumulative Exchangeable Preferred Stock, Series One (the "15%

Preferred Stock" or the "Redeemable Preferred"). The Senior Term Loans, the Divestiture Term Loans and the Revolving Credit Facility under the Credit Agreement are collectively known as the "Permanent Financing Facility." Upon consummation of the Merger, the Company became the obligor under the Credit Agreement.

Effective as of funding of the Term Loans, the Banks received, to the extent practicable, a security interest in all of the assets of the Company, except that no liens were placed upon certain retail facilities intended to be sold or already encumbered, properties outside the United States, the stock of Citgo and those other assets subject to specific pledge and assignment restrictions.

The Credit Agreement contains a number of financial covenants including ratios relating to Adjusted Senior Indebtedness to Subordinated Indebtedness, minimum interest coverage, minimum fixed charge coverage and maximum total debt. There is also a limitation on capital expenditures by the Company and various other covenants limiting the Company's ability to incur indebtedness or other liabilities, grant liens, make or guarantee loans, or make certain investments. The Credit Agreement also requires the Company to comply with various reporting requirements and limits the Company's ability to enter into certain transactions with shareholders and affiliates, engage in sales and leasebacks, and amend the terms of its charter or bylaws or the terms of any subordinated debt. These covenants contain exceptions which are customary in leveraged acquisition financing credit agreements, as well as exceptions consistent with the specific nature of the business and financial operations of the Company.

The Company intends to concentrate its efforts on its convenience retailing operations, which accounted for approximately 95 percent of total revenues in 1987. The Company intends to sell several of its other businesses and certain assets relating to its convenience store business (the "Divestitures") to generate cash to be used to satisfy a portion of its debt service obligations under the Credit Agreement incurred in connection with the Merger.

The Company, with executive offices at 2828 North Haskell Avenue, Dallas, Texas 75204 (telephone (214) 828-7011), was incorporated in Texas in 1961 as the successor to an ice business organized in 1927. Unless the context otherwise requires, the terms "Company," "Southland" or "registrant" as used herein include The Southland Corporation and its subsidiaries and predecessors.

The Company's 7-Eleven trademark has been registered since 1961 and is well-known throughout the United States and in many other parts of the world. Other trademarks and service marks owned by the Company include Super-7, Chief (which is used in connection with Chief Auto Parts) and Reddy® (which is used in connection with Reddy Ice). The trademarks and service marks owned by Citgo include Citgo and Quik Mart. Numerous other trademarks cover individual dairy products, frozen confections, fast food items and snacks manufactured by the Company. Southland anticipates that in most cases the trademarks traditionally associated with the business operations to be divested (other than 7-Eleven stores) will be sold with the divested operations.

In 1987 Southland's activities were divided into the following two business groups: Convenience Retailing and Food Processing and Manufacturing. In addition, the Company owns a 50-percent equity interest in Citgo. For purposes of this report, the Company's business is divided into (a) "Continuing Operations" which includes convenience retailing, the five distribution centers and the six food processing centers and (b) "Operations Being Divested", which includes the food processing and manufacturing businesses (other than the six food processing centers) and Chief Auto Parts. The Company also will retain its 50-percent equity interest in Citgo.

CONTINUING OPERATIONS

Convenience Retailing

7-Eleven Stores. The 7,818 7-Eleven convenience stores included in the Company's operations at December 31, 1987, and 521 stores operated by area licensees were located in 49 states, the District of Columbia, and five provinces of Canada. Such stores are operated principally under the name

7-Eleven. During 1987, the Company opened or acquired 445 convenience stores, including 39 stores acquired in the Midland/Odessa, Texas area from National Convenience Stores Incorporated ("NCS") and 25 Quik Marts that were converted to 7-Eleven stores. This resulted in a net increase of 146 7-Eleven convenience stores due to the relocation of 64 stores, the closing of 195 stores (due to changing market patterns and lease expirations) and the sale of 40 stores to third parties in market divestitures.

As part of the Divestitures in connection with the Merger, the Company announced its plan to divest approximately 1,000 operating convenience store properties and, as part of this program, on January 21, 1988, the Company sold 402 properties, including 270 operating 7-Eleven convenience stores and related assets owned or leased by the Company in or around Houston, Texas, to NCS. In addition, the Company and The Circle K Corporation ("Circle K") signed a letter of intent on February 29, 1988, pursuant to which Circle K will acquire 473 operating 7-Eleven stores, as well as related properties, in 10 states. The sale is subject to completion of a definitive agreement and governmental approval. In addition, on March 11, 1988, the Company and FFP Operating Partners, L.P. ("FFP") signed an agreement for FFP to acquire 21 stores in Missouri. The Company is also intending to sell approximately 250 other 7-Eleven stores as part of the Divestitures.

The Company's convenience stores are extended-hour retail stores, emphasizing convenience to the customer and providing groceries, take-out foods and beverages, gasoline, dairy products, non-food merchandise, specialty items and incidental services. The Company's retailing operations are influenced favorably by warm weather, as a large part of the Company's product mix is concentrated in items that are consumed during periods when leisure-time activities are more prevalent.

The 7-Eleven stores, which have one of the most recognized names in the United States among consumers, have a strong retail base, serving, as of December 31, 1987, more than 8,000,000 customers a day. The Company is presently seeking to build on its customer base through expansion of fast food programs, customer services and self-service gasoline.

Generally, the stores are open every day of the year and are located in neighborhood areas, on main thoroughfares, in shopping centers, or on other sites where they are easily accessible and have ample parking facilities for quick in-and-out shopping. During 1987, the vast majority of stores operated 24 hours a day, with virtually all of the Company's stores open at least from 7 a.m. until 11 p.m. The Company emphasizes personal, courteous service and clean, modern stores. The stores attract lunch-time customers, early and late shoppers, weekend and holiday shoppers and customers who may need only a few items at any one time and desire rapid service.

Typical stores contain approximately 2,400 square feet, carry more than 3,000 items, and have distinctive and easily recognizable exterior designs and signage. To maintain their modern appearance and accommodate new merchandising programs, the Company has had a program for continual remodeling of older stores; however, under the Credit Agreement it is anticipated that major remodeling will be limited in the immediate future. A flexible policy in both layout and product mix is maintained to appeal to regional preferences. Although most of the items sold are nationally or locally advertised brands, the Company continues to carry certain private-label products. Fast foods and a wide variety of seasonal items are also sold at many locations. Prices on most items are somewhat higher than in supermarkets; however, part of the Company's marketing approach has been to emphasize competitive pricing of products that will attract customers, including gasoline, milk, carton cigarettes and case beer, and to expand its selection of high-quality fast foods and customer services. In recent years, the Company expanded its competitive pricing policy to include additional items in certain markets. Substantially all convenience store sales are for cash (including sales for which checks are given), although major credit cards are accepted in most markets along with the "Citgo Plus" credit card.

In certain areas where stores are located, state or local laws limit the hours of operation or the sale of certain products, the most significant of which limit or govern the sale of alcoholic beverages and, along with federal regulations, the sale of gasoline. State and local regulatory agencies have the

authority to approve, revoke, suspend or deny applications for and renewals of permits and licenses relating to the sale of alcoholic beverages or to seek other remedies. In most states, such agencies have discretion to determine if a licensee is qualified to be licensed, and denials may be based on past noncompliance with applicable statutes and regulations as well as on the involvement of the licensee in criminal proceedings or activities which in such agencies' discretion are determined to adversely reflect on the licensee's qualifications. Product categories that are affected by these types of regulations are alcoholic beverages, tobacco, lottery tickets and other similarly state-regulated products. Such regulation is subject to legislative and administrative change from time to time.

In 1983, the Company began a program to install automatic teller machines (ATMs). By December 31, 1987, ATMs were installed in approximately 1,800 locations, and the Company had entered into agreements for the installation of ATMs at additional locations. In addition, electronic money order machines had been installed in 6,500 stores by year end. During 1987, the Company expanded its program of videocassette rentals to 6,450 7-Eleven stores, offering a 200-tape selection including many of the most frequently requested movie titles.

On March 4, 1988, the Company sold the assets of the Company's "MovieQuik" videocassette rental division to Cevaxs U.S. Corporation ("Cevaxs") for approximately $52 million. As part of the transaction with Cevaxs, the Company entered into a nine-year distribution agreement with Cevaxs under which Cevaxs will operate the videocassette rental system in approximately 4,100 of the Company's 7-Eleven convenience stores.

The Company's fast food program was expanded both geographically and in product choice during 1987. As of December 31, 1987, freshmade deli-style sandwiches were prepared on premises at 4,500 locations, freshly prepared hot dogs and nachos were available at 6,700 locations and pizza was served at over 650 locations. 7-Eleven's proprietary programs including "Get Hot", which features a variety of hot sandwiches, was available at 2,900 locations and "The Works", offering an expanded condiment bar to complement the Company's other sandwich programs, was available at over 1,000 locations. In addition, during 1987, the Company began selling "Dunkin' Donuts" and Winchell's branded doughnuts at selected locations and, by March of 1988, had expanded the program to over 800 stores.

In 1987, the Company sold approximately 2 billion gallons of gasoline at retail at 3,545 7-Eleven stores and other Southland self-serve outlets. In early 1986, the Company implemented plans to offer Citgo-branded gasoline at 7-Eleven gasoline locations, and this branding program has been completed in 2,700 7-Eleven stores east of the Rocky Mountains. In addition, there are over 875,000 "Citgo Plus" credit card accounts. Holders can use the "Citgo Plus" credit cards to finance limited purchases of gasoline and merchandise at 7-Eleven stores and Citgo-branded distributor outlets, as well as certain repair services and automotive equipment at the Citgo-branded distributor outlets. Since 1986, Southland and Mobil Oil Corporation have jointly developed several sites at which the oil company's branded gasoline is offered and Southland operates a convenience store.

At December 31, 1987, the Company's dairies served more than 5,700 of the Company's convenience stores, supplying a large portion of the dairy products sold by them in 1987 (see "Dairies Group" for a discussion of the planned sale of the dairies). In addition, the Company's five regional distribution centers supplied 74 percent of the Company's convenience stores in 43 states, the District of Columbia and Puerto Rico with a substantial amount of those stores' merchandise, excluding gasoline. During 1987, fast foods and ice products were also supplied by the Company wherever practical. Products not available from the Company are purchased from various independent wholesalers, distributors and rack jobbers. Inventory is purchased by each store based upon historical sales and the buying habits of customers in each specific area. Franchisees are required only to carry merchandise of a type, quality, quantity and variety consistent with the 7-Eleven image and, except for consigned merchandise, franchisees are not required to purchase merchandise from the Company or vendors it recommends, or to sell their merchandise at prices suggested by the Company.

The Company does not record sales on the basis of product categories. However, based upon the total dollar volume of store purchases, management estimates that the percentages of its 7-Eleven convenience store sales in the United States by principal product categories for the last five years were as follows:

	Years Ended December 31				
Product Categories	**1987**	**1986**	**1985**	**1984**	**1983**
Gasoline	22.7%	22.1%	25.5%	24.8%	25.5%
Tobacco Products	16.3	15.8	14.8	14.4	13.8
Beer/Wine	11.2	11.7	11.0	11.4	11.8
Soft Drinks	10.7	10.9	10.6	10.5	10.4
Food Service	8.4	8.1	5.6	5.3	4.6
Groceries	8.3	8.6	10.1	10.5	10.5
Non-Foods	6.1	6.4	7.1	7.0	7.5
Dairy Products	5.1	5.2	5.3	5.7	5.7
Candy	3.7	4.0	3.9	4.0	3.9
Baked Goods	3.3	3.5	3.4	3.6	3.5
Health/Beauty Aids	2.4	2.6	2.7	2.8	2.8
Customer Services	1.8	1.1	—	—	—
Total	100.0%	100.0%	100.0%	100.0%	100.0%

To increase cash flow available to service the Company's increased indebtedness following the Merger, the Company intends to reduce capital expenditures substantially below the amounts expended during recent years. In addition, under certain circumstances, the Credit Agreement may limit the Company's ability to make capital expenditures. As a result, the Company expects to expend fewer resources on remodeling existing convenience stores and to limit plans for new store openings. The Company's high degree of leverage could significantly limit its ability to make acquisitions or take advantage of significant business opportunities that may arise.

Franchises. Of the 7,818 7-Eleven convenience stores included in the Company's operations at December 31, 1987, 3,064 were operated by independent franchisees under the Company's franchise program for individual 7-Eleven stores. Sales by stores operated by franchisees (which are included in the Company's net sales) were $3,004,125,000 for the year ended December 31, 1987.

In its franchise program for individual 7-Eleven stores, the Company selects qualified applicants and trains the individuals who will participate personally in operating the store. The franchisee pays the Company an initial fee to cover certain costs including training, an allowance for travel, meals and lodging for the trainees and other costs relating to the franchising of the store. Under the current franchise agreement the Company leases or subleases to the franchisee a ready-to-operate 7-Eleven store that has been fully equipped and stocked. The Company bears the cost of acquiring the land, building and equipment, as well as most utility costs and property taxes.

The franchisee pays for all business licenses and permits as well as all selling expenses, including: payroll; inventory and cash variations; supplies; inventory, payroll and other business taxes; certain repairs and maintenance; and other controllable in-store expenses and is required to invest an amount equal to the cost of the store's inventory and cash register fund. The Company will finance a portion of the cost of business licenses and permits and of the investment in inventory, as well as continuing operating expenses and purchases of inventory. The Company is also studying the feasibility of introducing additional types of franchising arrangements in the future.

Under the current franchise agreement the Company shares in the gross profit of the store (ranging from 50% to 63%, adjusted if necessary to assure the franchisee a specified gross income before selling expenses, depending on the cost of the location and hours of store operation) based on all sales of merchandise and services except those on which the Company pays the franchisee a

commission (such as consigned gasoline). The Company's share of gross profit is its continuing charge to the franchisee for the license to use the 7-Eleven operating system and trademarks, for use of the store premises and equipment and for continuing services provided by the Company. These services include merchandising, advertising, bookkeeping, store audits, business counseling services, training seminars and preparation of financial statements. Other optional services are available from or through the Company for additional fees.

The franchise may be terminated by the franchisee at any time or by the Company for the causes, and on notice, as specified in the franchise agreement and as provided by applicable law. In the event of expiration or termination of the franchise, the Company has the right to (i) acquire the franchisee's interest in inventory of a type, quantity, quality and variety consistent with the 7-Eleven image and other tangible assets in the franchise business; and, (ii) take possession of the real property on which the store is located, and the franchisee has no continuing lease obligation.

Many states in which the Company franchises individual 7-Eleven stores have enacted legislation governing the offer, sale, termination and/or renewal of franchises, and the Federal Trade Commission has adopted a trade regulation rule regarding required disclosures to potential franchisees. These requirements are subject to amendment and similar legislation is pending in other states.

Area Licensees. As of December 31, 1987, the Company had granted area licenses to 10 companies which were operating 521 convenience stores using the 7-Eleven system and name in certain areas of Alaska, Arkansas, Indiana, Iowa, Kansas, Kentucky, Maine, Michigan, Minnesota, Missouri, Montana, Nebraska, New Hampshire, North Dakota, Ohio, Oklahoma, Pennsylvania, South Dakota, West Virginia, Wisconsin and Wyoming. Similar license agreements cover the operation of 3,245 7-Eleven stores in Japan, 210 in Hong Kong, 168 in Taiwan, 121 in Australia, 49 in the United Kingdom, 63 in Singapore, 54 in Malaysia, 13 in Norway, eight in the Philippines, two each in The Republic of Ireland and Panama, and one each in Guam, Puerto Rico and Spain. In addition, in late 1987, the Company entered into a license agreement for the operation of 7-Eleven stores in Indonesia, although at year end no stores were in operation. In connection with the granting of area licenses in The Republic of Ireland, Norway, Puerto Rico, Spain and the United Kindgom, the Company acquired a minority equity interest in those area licensees.

The Company is considering other countries where licensing is feasible. Stores operating under area licenses are not included in the number of Company operating units, and their sales are not included in the Company's revenues. Net profit from initial fees paid for area licenses and continuing royalties based on the sales volume of the stores are included in Other Income. In addition, the Company has announced that it entered into a financing arrangement to monetize its Japanese license royalties to generate funds for its debt service obligations. The financing is collateralized by the Company's Japanese 7-Eleven trademarks and the right to receive royalties from the Japanese licensee during the term of the loan.

International. At December 31, 1987, Svenska/7-Eleven AB, the Company's Swedish subsidiary, operated 65 stores in Sweden which are operated under the 7-Eleven/näröppet name. An additional store was opened after year end. The Company also has an equity interest in over 100 convenience stores in Mexico (90 as of year end) operated by an affiliate under the name Super Siete, featuring merchandise and service similar to 7-Eleven stores. Sales by these stores are not included in Southland's revenues, but Southland's equity in their operating results is included in Other Income and has not been material.

High's Dairy Stores. On December 31, 1987, the Company operated 319 High's Dairy Stores located primarily in Maryland and Virginia, which are similar in size and location to 7-Eleven stores with a product mix that focuses on a variety of dairy products.

Quik Mart and Super-7. At December 31, 1987, 113 Quik Mart and Super-7 units were in operation in fourteen states. A typical Quik Mart is a high-volume gasoline outlet combined with a

mini-convenience store ranging in size from 300 to 1,600 square feet of sales space stocked primarily with snack food, candy, cold drinks and other immediately consumable items, while a Super-7 is a high volume, multi-pump self-service gasoline dispensing operation.

Distribution Group. The Company has five regional distribution centers, located in California, Florida, Illinois, Texas and Virginia, that serve retail and food service customers in 43 states, the District of Columbia and Puerto Rico, including a total of 6,193 7-Eleven and High's Dairy Stores and Quik Mart locations, 1,187 food service outlets and 2,253 other convenience stores and retail units. During 1987, the distribution centers' sales increased 9.4 percent, with outside sales now representing approximately 22.5 percent of their total sales. The Distribution Group also operates four relay stations (one each in Delanco, New Jersey; Roanoke, Virginia; Pompano, Florida; and Atlanta, Georgia) to facilitate deliveries.

One of the distribution centers' most important competitive advantages is their ability to fill less-than-case-lot orders, allowing customers, such as convenience stores, to improve inventory turnover, maintain fresher merchandise and better utilize limited selling space.

Food Centers. The Company's Food Centers, located at each of four regional Distribution Centers and in Salt Lake City, Utah, and St. Louis, Missouri, produce sandwiches, French bread pizzas, burritos, snack cakes, sauces and other fast food items primarily for distribution to the Company's convenience stores. In addition, the Fast Foods Division, directly and through distributors, sells sandwiches and other food products under the Company's labels primarily to other retailers and institutional customers. Principal brands include "Deli Shoppe®" (sandwiches), "Casa Buena®" (burritos and sauces), "Italini®" (pizzas), "Aunt Bea's®" (cakes and sweet snacks), "Smileys®" (sandwiches), and "Sonritos®" (burritos). Product lines were expanded during 1986 with the introduction of several new products, including foil-wrapped sandwiches, sheet brownies, iced tea syrup, and specialty burritos and sandwiches for school foodservice needs. In 1987, the food centers expanded their product line with multi-packs of pizzas, sandwiches and burritos, a new non-carbonated frozen juice product, individual entrees for vending machines and a new beef and chicken chimichanga. During the five years ended December 31, 1983 through 1987, approximately 68%, 67%, 62%, 53% and 48%, respectively, of the food centers' sales were intracompany. Most of the raw materials used by the food centers are purchased from various independent sources, and the balance are purchased from other operations of the Company.

Event Ticketing. The Company's Rainbow Ticketmaster Division, acquired in 1985, sells computer-generated tickets for entertainment and sporting events throughout Texas and, starting in May, 1988, will begin operations in Florida.

Citgo Petroleum Corporation

Citgo Petroleum Corporation is a petroleum and lubricants refining and marketing operation. It is comprised of Citgo and its subsidiaries which include Cit-Con Oil Corporation (65 percent owned), Citgo Pipeline Company, Citgo International Supply Company, Citgo Caribbean Corporation, and minor subsidiaries. The Company acquired Citgo on August 31, 1983 and, on September 30, 1986, sold a 50-percent equity interest in Citgo to Propercit, S.A. a subsidiary of Petroleos de Venezuela, S.A. ("PDVSA"), the Venezuelan national oil company. This interest has been transferred by Propercit to another subsidiary of PDVSA. The Company's former Gasoline Supply Division, which included Foremost Petroleum Company of Texas, Inc., was combined with Citgo at the beginning of 1986.

Citgo's operations are divided along three major functional lines, as follows:

Refining Operations — These operations include a crude oil refinery (the "Refinery"), located near Lake Charles, Louisiana, and a 65 percent interest in a lubricants refinery (the "Lubricants Refinery") adjacent to the Refinery (Cit-Con Oil Corporation). The Refinery, which is one of the largest in the United States, has a rated crude oil throughput capacity of 320,000 barrels per calendar day ("BPD"). The Refinery's deep conversion capability enables less expensive, heavy sour crude oils to be processed efficiently into premium quality transportation fuels. The Refinery also processes light, low-sulfur, domestic crude oils to provide quality feedstocks for the Lubricants Refinery.

The processing operations of the Refinery include atmospheric and vacuum fractionation, hydrocracking, catalytic reforming, catalytic cracking, alkylation, coking, hydro-desulfurization, aromatics recovery, treating, blending, sulfur recovery, sulfuric acid manufacture and propylene fractionation. Construction of a new 2,400 BPD MTBE (methyl tertiary butyl ether) unit was completed in 1987 which processes internally produced feedstock and increases Citgo's ability to produce high quality premium unleaded gasolines by approximately 10,000 BPD (15%) from 1986. A capital project to increase the propylene fractionation unit production capacity by 500 BPD (14%) was completed during the first quarter of 1987.

Each barrel of crude oil processed at the Refinery yields over 90 percent light fuels consisting of gasoline, jet fuel, diesel, and No. 2 fuel oil. Gasoline yield per barrel of crude oil processed is approximately 70 percent.

The following table sets forth annual production data for the Refinery.

	1987	1986	1985
		(000s BPD)	
Gasoline			
Regular	16	13	19
Unleaded	86	109	83
Super unleaded	73	39	36
Total	175	161	138
Distillates			
Kerosene	3	4	4
Diesel and No. 2 fuel oil	13	18	22
Jet and turbine	36	35	34
Total	52	57	60
General refinery products(a)	35	39	21
Total	262	257	219

(a) Includes products from intermediate feedstocks.

Operating under the 20-year supply agreement signed with PDVSA in 1986, the Refinery received about 100 MBPD ("thousand barrels per day") of heavy sour and 30 MBPD of light sour crude oils from Venezuela in 1987. In addition, Citgo significantly increased its acquisitions of heavy sour crudes from PEMEX, the national oil company of Mexico, to about 45 MBPD by the end of 1987. These Latin American crude oil supplies, augmented by stable and significant domestic lease purchases from Occidental Petroleum Corporation and production from certain of its affiliated companies and other domestic producers, leaves only 10 to 15 percent of Citgo's feedstock requirements to be acquired on the spot market.

The following table presents annual statistics on crude runs for the Refinery.

	1987	1986	1985
		(000s BPD) (Except percentages and cost)	
Domestic	62	66	85
Foreign	179	172	119
Total Runs	241	238	204
% Heavy Sour Crude Runs	59	52	27
Crude Cost (per barrel)	$16.85	$14.28	$26.42

Over 70 percent of Citgo's branded gasoline sales were supplied from gasoline manufactured at the Refinery. During 1987, Citgo entered into new long-term gasoline purchase contracts with PDVSA (Venezuela) and Neste (Finland).

Citgo also has a 65-percent interest in the Lubricants Refinery, which is the fourth largest paraffinic lubricant and refined wax refinery in North America. The Lubricants Refinery's capacity is 10,000 BPD of finished lubricants; 960 BPD of finished wax; and 900 BPD of unfinished wax.

During 1987, a $17 million Process Computer Control project was placed in service at the Lubricants Refinery. This project modernized the refinery's instrumentation and consolidated control in an ultra-modern control center.

The following table sets forth the Lubricants Refinery's annual production and major customers.

	1987	1986	1985
		(BPD)	
Production:			
Lubricants	8,917	8,786	8,794
Waxes	1,237	1,430	1,462
Total	10,154	10,216	10,256
Sales:			
Citgo	6,612	6,641	6,673
Other	3,542	3,575	3,583
Total	10,154	10,216	10,256

Citgo also owns a compounding plant in Cicero, Illinois, which has the capacity of blending and/or packaging 50 million gallons of lubricant products yearly (based on a one-shift operation).

The Lubricants Refinery's base oils output, in addition to supplying Citgo's blending and packaging plant at Cicero, Illinois, is shipped to any of 20 full-line contract blending and packaging facilities or other specialized source points located throughout the country for further processing.

Marketing Operations — These operations include both wholesale and retail marketing of petroleum products for motor vehicles and commercial, residential and industrial use.

At the end of 1987, there were approximately 7,500 Citgo-branded retail outlets, almost 65 percent of which were distributor facilities, an increase of 1,200 outlets since year-end 1986.

In 1987, Citgo acquired a 1,300,000-barrel terminal in Albany, New York, and a 50-percent interest in a 360,000-barrel terminal near Milwaukee, Wisconsin, in addition to adding 106,000 barrels of capacity at its Syracuse, New York, facility. Citgo now wholly or partially owns 42 refined product terminals throughout its primary market areas, including its aviation fuel terminal at Miami International Airport, with a combined storage capacity of 18 million barrels. During 1987, Citgo completed the installation of an automated terminal system at its product terminals which significantly enhanced operations and control of inventory storage and product movement. Citgo augments its equity network with purchases and exchanges of product at over 300 other refined product terminals.

The Company has a 20-year product purchase agreement with Citgo, entered into in 1986, to buy gasoline at market-related prices, with minimum required annual purchases based, in some cases, on the Company's total purchases of gasoline for retail sale.

During 1987, Citgo introduced its new 92 octane "The Performer" premium unleaded gasoline with CDX-100 detergent. Sales of premium unleaded gasoline to wholesale branded distributors increased to 21 percent of total gasoline sales by year-end.

Over one million tons of petroleum coke were produced at the Refinery and sold during 1987. The majority of shipments were made through the Lake Charles Coke Handling Terminal (which is 50 percent owned by Citgo), while the Port of Lake Charles handled the remainder. Other industrial product sales included propylene, propane, sulfur, and residual fuels.

Lubricant sales include about 350 types and grades of automotive and industrial lubricants and waxes. During the past three years, a period of declining demand for finished lubricants in the industry, Citgo increased sales of finished lubricants by 12 percent and refined wax by 33 percent. Sales to branded distributors increased 26 percent during the same time period. At year-end 1987, 60 percent of Citgo's

finished lubricants were sold through distributors. Citgo also maintains purchase and resale arrangements with major tire, battery and accessory manufacturers. Principal markets include distributors and industrial, commercial and mass merchandising customers.

The following table sets forth Citgo's annual sales by product category.

Product Categories	1987	1986	1985
		(Millions of Gallons)	
Gasoline:			
Unleaded plus	34.4	6.5	5.3
Super unleaded	1,030.2	700.3	381.6
No lead	2,775.7	2,676.6	1,746.6
Regular plus	10.2	19.7	35.2
Regular	1,072.1	1,657.2	1,284.4
	4,922.6	5,060.3	3,453.1
Distillates:			
Diesel fuel	177.7	471.9	166.1
No. 2 heating fuel	327.2	579.6	345.3
Turbine fuel	817.8	874.1	703.1
	1,322.7	1,925.6	1,214.5
Propylene	50.7	50.4	42.7
Other(a)	850.3	815.3	532.1
Total	7,146.3	7,851.6	5,242.4

(a) Includes lubricants, antifreeze, and refinery co-products and heavy residual fuels such as petroleum coke, No. 6 fuel oil, decant oil and various feedstocks.

The following table sets forth information with respect to types of customers of Citgo for 1987.

Customers	Amount (Millions of Gallons)	%
Distributors/resellers	3,801.7	53.2
Retail marketing	46.1	.6
Airlines and government	618.4	8.6
Sales to Southland	1,890.7	26.5
Other	789.4	11.1
Total	7,146.3	100.0%

Transportation Operations — These operations include a 1,300-mile common carrier crude oil gathering and transportation network and ownership interests in two common carrier crude oil trunkline systems, which total more than 250 miles, through one of its subsidiaries, Citgo Pipeline Company. Citgo, through another of its subsidiaries, Citgo Pipeline Investment Company, owns shares in three common carrier crude oil pipeline companies with aggregate mileage of approximately 6,000 miles and six common carrier refined products pipeline companies with aggregate mileage of approximately 8,000 miles. Citgo's transportation system is supported by a crude oil dock facility and a crude oil tank farm, both located near the Refinery, which have approximately four million barrels of storage capacity and by a system of terminal facilities with substantial storage capacity, including products terminals at Linden, New Jersey; Petty's Island, New Jersey; East Chicago, Indiana; Braintree, Massachusetts; and Albany, New York, each with storage capacities exceeding one million barrels.

Common carriers engaged in the interstate transportation of crude oil and refined products are subject to regulation by the Federal Energy Regulatory Commission (the "FERC") under the Interstate Commerce Act (the "ICA"). State regulatory agencies govern the intrastate transportation of crude oil and refined products. A common carrier's pipeline tariffs must be just and reasonable, equally applicable to owners and non-owners and, under the ICA, must be filed with the FERC before taking effect. In

addition, common carrier pipelines are required to offer their facilities on a non-discriminatory basis to all shippers meeting the pipeline's rules and regulations.

Corporate

Cityplace. The Company owns approximately 160 acres of land known as "Cityplace" located immediately north of Dallas' central business district and surrounding a proposed major stop on the city's planned mass transit system. In January 1984, Cityplace Development Corporation was formed by the Company to manage the Cityplace project. The Company's current headquarters and a 42-story office tower (the "East Tower") under construction on an approximately 12-acre tract adjacent to the east side of Dallas' Central Expressway are both located within Cityplace. The East Tower is scheduled for completion in late 1988.

In early 1987, Cityplace Center East Corporation, an indirect wholly owned subsidiary of the Company, issued $290 million of 7⅞% notes due 1995 to finance construction of the East Tower, including an underground parking garage and other related facilities. The debt, which is nonrecourse to the Company, is supported by a letter of credit issued by The Sanwa Bank Limited and is secured by a first deed of trust lien on the East Tower. The Company has executed a lease for the entire East Tower (the "Lease") and its rental payments under the Lease are calculated to cover debt service on the public debt. The Cityplace notes have remained outstanding in accordance with their terms following the Merger. There are no restrictions in the Lease on the Company's ability to sublease space in the East Tower, provided that the Company remains principally liable for rental obligations under the Lease.

Original plans called for the Company to be the only occupant of the East Tower. However, in light of reduced space requirements due to the Divestitures and in order to reduce operating expenses following the Merger, the Company currently does not intend to occupy the entire East Tower upon completion. The Company intends to sublease approximately one half of the East Tower to third parties.

In February 1987, the Company submitted to the City of Dallas a zoning application for the approximately 135 acres of land in Cityplace not previously rezoned. This application, currently pending, contemplates various uses within Cityplace, including office, retail, hotel, and multi-family housing.

Citijet. In April 1982, Southland purchased a long-term leasehold interest in an 18-acre tract at Love Field, Dallas, Texas. In 1984, Southland opened a fixed-base operation known as "Citijet" to service general aviation customers, as well as the Company's requirements, providing fuel facilities, hangar space, food service and other aviation-related services. The terminal facility includes passenger and pilot lounge areas, a restaurant open to the public, and office space. In March 1986, as part of a financing arrangement, the Company assigned its long-term lease to a third party and sub-leased back the 18-acre tract.

OPERATIONS BEING DIVESTED

Food Processing and Manufacturing

In connection with the Merger, the Company intends to divest all its food processing and manufacturing operations described below and, on February 17, 1988, announced that it had entered into an agreement with MorningStar Foods, Inc. to sell the Dairies Group. Agreements have also been announced for the sale of Tidel Systems and Reddy Ice.

Dairies Group. At December 31, 1987, the Dairies Group processed and distributed milk, ice cream, frozen confections and related products through 24 plants and 57 distribution points (including points at each processing plant) with sales in 46 states, Guam, the Caribbean and Japan. The related products include cottage cheese, dips, eggnog, hard cheeses, juice-based drinks, juices, sour cream, toppings, ultra-pasteurized creams and yogurt. In addition, the 24 plants include an ice facility and dry-and-cold storage operation and a plastic bottle production plant. Substantially all of the required raw milk is purchased through cooperative marketing associations, with the remainder purchased from independent producers.

The Dairies Group's principal brands include Adohr Farms®, Bancroft®, Cabell's®, Embassy®, High's, Merritt®, Oak Farms®, Specialty Products, Velda Farms® and Wanzer®. In order to develop national recognition of its dairy products, while preserving local brand names, the Dairies Group markets most of its products under a uniform package design. Other brand names used by the dairies are Mission San Juan® (natural fruit drinks), Barricini® (premium ice cream), Farmfield® (fruit juices and drinks), Naturally Yours® (yogurt) and Trimline® (cottage cheese).

Merritt Foods, along with the Specialty Products Division, produces a wide variety of frozen confections that are distributed throughout the United States under several distinctive owned trademarks and also under private labels for others. In addition, the Dairies Group is the exclusive manufacturer and distributor of the Dole "Fruit 'n Juice" bar, Dole "Fruit Sorbet" and the Dole "Fruit and Cream" bar, which are natural fruit-flavored, low-calorie, frozen confections and of "Chipwich," an ice cream sandwich made with a variety of cookies and ice creams. The dairies contemplate introducing additional Dole products in 1988.

The following table sets forth information with respect to customers and product categories of the Dairies Group for the last five years.

	Years Ended December 31				
Customers	**1987**	**1986**	**1985**	**1984**	**1983**
Wholesale	55%	55%	53%	52%	51%
Intracompany	40	40	42	43	42
Distributors and others	5	5	5	5	7
Total	100%	100%	100%	100%	100%

	Years Ended December 31				
Product Categories	**1987**	**1986**	**1985**	**1984**	**1983**
Milk, cottage cheese and other food items	73%	71%	72%	75%	79%
Ice cream and related products	27	29	28	25	21
Total	100%	100%	100%	100%	100%

During 1987, the Company sold its ice cream plant in Atlanta, Georgia. In addition, at the end of 1987 and beginning of 1988, two ice cream plants in Memphis, Tennessee, and Alexandria, Virginia, were closed. Also closed was a juice plant in Watsonville, California, with its production moved to the dairies' new facility in Sebastopol, California.

The dairy industry is subject to regulation by the U.S. Department of Agriculture and/or state agencies with respect to minimum prices paid to milk producers and license requirements and other controls by state and local health authorities and other regulatory agencies. Such regulation is subject to legislative or administrative change from time to time.

Chemical/Food Labs. The Company's Chemical/Food Labs Division produces a variety of food ingredients and specialty chemical products. It supplies Southland's operations with certain sanitation chemicals, food flavorings and other ingredients used in dairy and other food products and distributes to outside customers items such as hair dyes, food stabilizers, flavors and preservatives, cleaning compounds and sanitizers, lubricants, food emulsifiers, surfactant compounds, pharmaceutical chemicals and chemical additives. In addition, the Division increased its sales of aseptically processed fruits and flavors which are used in juices and other fruit-flavored products. During the five years ended December 31, 1983 through 1987, approximately 21%, 24%, 26%, 30% and 35%, respectively, of the Division's sales were intracompany. Raw materials are purchased from various independent sources. The chemical industry is subject to regulation by the federal Environmental Protection Agency and similar state and local agencies with respect to protection of the environment.

Such regulation is subject to legislative or administrative change from time to time. (See "Environmental Matters," below.)

Reddy Ice. During 1987, the Company sold commercial and packaged block and processed ice under the trade name Reddy Ice in Florida, Nevada, Oklahoma, Texas and Utah and sold cut and packaged firewood under the name Reddy Wood in Texas. In addition, Reddy Ice periodically sells its products in Arizona, California, Kansas and Louisiana. At December 31, 1987, ice plants were located one each in Florida and Nevada and six in Texas. During the five years ended December 31, 1983 through 1987, approximately 32%, 34%, 35%, 34% and 28%, respectively, of the Reddy Ice Division's sales were intracompany.

Tidel. Tidel manufactures a variety of electronic and mechanical equipment for use primarily by retail sales and distribution companies. Starting in the late 1970s with the introduction of a microprocessor-based cash control system, Tidel has expanded its product line to include several other products, the latest being a gasoline tank monitoring system which uses a combination of ultrasonic and microprocessor technology to provide vital data regarding gasoline inventories. During the five years ended December 31, 1983 through 1987, approximately 50%, 39%, 39%, 51% and 26%, respectively, of Tidel's sales were intracompany. Outside customers consist of a wide variety of retailers, including convenience stores and fast food establishments.

Pate Foods. Pate Foods, acquired by the Company in mid-1983, is located in South Beloit, Illinois. Pate produces a line of corn-based products, cheese puffs and popcorn under its own brand name and private labels for outside customers and distributed these products in 20 states during 1987. Pate Foods' customers include supermarket chains such as Eagle Food stores and Gateway Foods, which together account for about 12 percent of Pate Foods' sales. In 1984 through 1987, intracompany sales accounted for approximately 5%, 18%, 31% and 26%, respectively, of Pate Foods' sales.

Keystone Pretzels. In May 1987, the Company acquired all the assets of Keystone Pretzel Bakery, Inc., in Lititz, Pennsylvania, including a recently constructed pretzel bakery that produces 200,000 pounds of packaged pretzels per week. Keystone manufactures both salted and unsalted pretzels in a variety of shapes and sizes. Since the acquisition, all sales have been to outside customers.

El-Ge Potato Chip. In 1984, the Company acquired El-Ge Potato Chip Co., Inc., located in York, Pennsylvania, one of the largest independent manufacturers of potato chips in the Northeast. El-Ge manufactures a full line of potato chip products under its own brand name as well as under generic and private labels. El-Ge's distribution area includes Delaware, the District of Columbia, Maryland, Michigan, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Virginia, West Virginia and Wisconsin. During 1987, the Company sold corn products manufactured by Pate Foods under the LG® label. El-Ge distributed pork rinds, onion rings, dips, and salty nuts under the El-Ge label and hand-cooked batch-style potato chips under the Senft® label. In 1984 and 1985, intracompany sales by El-Ge, both directly and through distributors, accounted for approximately 18% and 19%, respectively, of its sales. In 1987, El-Ge continued to sell its products through distributors to 7-Eleven stores and other customers. Direct intracompany sales by El-Ge in 1987 accounted for about 1% of El-Ge's sales, while sales to 7-Eleven through distributors accounted for about 18.4% percent.

Chief Auto Parts

As of December 31, 1987, the Company had 469 operating Chief Auto Parts stores. The Company signed a definitive agreement on December 24, 1987, to sell its Chief Auto Parts Division to Chief Auto Parts, Inc., a new corporation formed by Chief's management and Shearson Lehman Brothers, acting as principal.

A typical Chief store is 3,700 square feet, open seven days a week and located in a neighborhood shopping center close to customers' homes or businesses. The older stores are smaller, with an average of 2,400 square feet. Store hours have been expanded to 16 hours per day, and in many markets, selected stores are open around the clock. The stores, which offer approximately 7,415 replacement parts and accessories, feature nationally known brands as well as private-label products.

OTHER BUSINESS INFORMATION ABOUT THE COMPANY

Research and Development

The Company (excluding Citgo) spent approximately $1,453,000 in 1983, $1,656,000 in 1984, $1,781,000 in 1985, $2,946,000 in 1986 and $2,482,000 in 1987, through the Chemical/Food Labs Division's Product Development Department, Tidel, the Research and Development and Technical Services Departments, the Corporate Marketing Department's concept research and other research activities relating to the development of new, and the improvement of existing, products and services. Citgo spent $534,000, $1,440,000, $1,476,000, $1,520,000 and $1,559,000, in the last four months of 1983, and the years ended 1984, 1985, 1986 and 1987, respectively.

Competition

Each of the Company's operations is conducted under highly competitive market conditions.

The Company's convenience retailing operations represent only a very small percentage of the highly competitive food retailing industry. Independent industry sources estimate that in the United States annual sales in 1987 for the convenience store industry were approximately $70 billion and that over 80,000 store units were in operation. The industry traditionally has narrow net profit margins. The Company's stores compete with a number of national, regional, local and independent retailers, including grocery and supermarket chains, other convenience store chains, oil company gasoline/mini-convenience "g-stores," and independent food stores, as well as variety, drug and candy stores. In sales of gasoline, the Company's stores compete with other food stores and service stations and generate only a very small portion of the gasoline sales in the United States. Each store's ability to compete is dependent on its location, accessibility and individual service. The Company attributes the success of its convenience retailing operations to the geographic spread of its stores, proper site selection techniques, merchandising, financial controls and advertising programs.

The Distribution Centers, which serve nearly all of the Company's retail convenience stores, compete with local and regional grocery wholesalers. The Distribution Centers also serve many accounts outside of the Company's operations, including several major restaurant chains, and in doing so, compete directly with other established product distribution networks. The Company believes that the ability to quickly fulfill orders for many items in less than full case lots affords the Distribution Centers a unique competitive advantage.

The Food Centers product lines of convenience foods, sauces, bakery products, and beverage syrups compete with other large foodservice processors and packagers who supply foods individually packaged for immediate consumption. The industry has enjoyed steady growth over the past several years due to various socioeconomic factors including the increasing number of working women, dual-income families, and single person households, and the growing demand for more leisure time. An industry annual growth rate of over 8% is projected through 1995. Food service is characterized by highly segmented operator groups, a highly competitive and complex distribution system, and a relatively low level of brand loyalty.

Citgo participates in the highly competitive gasoline refining and marketing industries, competing both to purchase available product and then, with other wholesalers and distributors of refined petroleum products, including independent and integrated oil companies, refiners and marketers, to resell to customers. Industry sources estimate that the demand for refined petroleum products in the United States in 1987 was approximately 254 billion gallons. Citgo's Refinery accounted for approximately 1.5 percent of the total refined products sold in United States markets during 1987 and is only one of 182 operating refineries in the United States as of January 1, 1988.

The Dairies Group has widespread distribution and competes with national and local dairy companies. The industry has been adversely affected in recent years due to the entry of new competitors, including major food companies in the ice cream business and farmers' cooperatives and retail

chains in the milk business. These factors have caused excess capacity at many plants, resulting in competitive pricing in the marketplace. Earnings are dependent on the maintenance of relatively large sales volumes and on efficiency of operation and distribution.

Cityplace, the Company's multi-use development in Dallas, Texas, is designed to provide office, retail, hotel and residential space both for use by the Company and lease to third parties. It is currently contemplated that, with the exception of space in the East Tower, construction of space available for lease to third parties will not begin until there is sufficient tenant interest and preconstruction lease commitments have been obtained. This project competes for tenants with other downtown, Oak Lawn, North Dallas and North Central Expressway luxury office space developments. The Dallas real estate market currently has many office and retail sites available for lease. It is anticipated that competition for tenants will remain strong in the Dallas commercial real estate market.

Environmental Matters

The operations of the Company are subject to various federal, state and local laws and regulations relating to the environment. Certain of the more significant federal laws that particularly relate to the Company's chemical and Citgo's petroleum refining and distribution operations are described below.

The Company is subject to the Clean Water Act, the Clear Air Act and the regulations promulgated thereunder. The implementation of these laws by the United States Environmental Protection Agency ("EPA") and the states will continue to affect the Company's operations by imposing increased operating and maintenance costs and capital expenditures required for compliance. Additionally, the procedural provisions of these laws can result in increased lead times and costs for major new facilities.

The Resource Conservation and Recovery Act ("RCRA") of 1976, as amended, affects the Company through its substantial reporting, recordkeeping and waste management requirements, thereby increasing the cost of all types of waste disposal. New regulations under RCRA are likely to prohibit certain types of waste disposal, further increasing Company costs for waste management. In addition, new statutory provisions enacted in 1984 impose additional requirements, including standards for underground fuel storage tanks and associated equipment, which may increase the costs of marketing petroleum products. In response to this legislation, and various state and local regulations, the Company has developed a comprehensive tank testing, repair and replacement program and has established a self-insurance program to address costs associated with leaks and spills from underground tank systems. In addition, Company facilities requiring waste management permits may be subject to broader and more costly cleanup responsibilities as a consequence of the 1984 amendments to RCRA.

The Comprehensive Environmental Response Compensation and Liability Act of 1980 ("CERCLA"), as amended, imposes additional taxes on crude oil, certain petroleum products and chemicals. This Act also creates the potential for substantial liability for the costs of study and cleanup of waste disposal sites and requires the reporting of certain releases into the environment. Recent court interpretation of this Act may result in joint and several liability even for parties not primarily responsible for hazardous waste disposal sites. As a consequence of past waste disposal on or off Company property, the Company may be potentially liable for cleanup costs at several sites which are being considered or which may be considered for Federal cleanup action under CERCLA. Additional requirements imposed by the Superfund Amendments and Regulations Act of 1986 may also result in additional reporting duties and may entail certain additional operating expenses.

The Safe Drinking Water Act, designed to protect public and private water supplies, regulates underground injection wells with respect to subsurface implacement of fluids.

The Toxic Substances Control Act ("TSCA") and the Federal Insecticide, Fungicide and Rodenticide Act regulate the manufacture, distribution, processing and use of chemicals, including pesticides, to avoid any unreasonable risk to human health or the environment. Included within the scope of TSCA are requirements on developing new chemicals, review and testing of existing chemicals, and specific rules on the use, handling and disposal of polychlorinated biphenyls.

Violation of any of these federal statutes or regulations or orders issued thereunder, as well as relevant state and local laws and regulations, could result in civil or criminal enforcement actions.

Current environmental projects and proceedings. In 1987, the Company completed construction of a stormwater management project at one of the Company's chemical facilities at a cost of approximately $5.4 million. This project was previously reported.

On April 30, 1987, the EPA issued a Notice of Violations ("NOV") to Citgo for alleged violations of the Clean Air Act and EPA's lead phasedown regulations. On December 16, 1987, Citgo and EPA entered into a Settlement Agreement under which Citgo agreed to pay a civil penalty of $80,000; contribute $20,000 to a non-profit organization; and retire 7,000,000 grams of lead credits.

In late 1986, EPA and Citgo entered into negotiations concerning alleged violations of Citgo's National Pollutant Discharge Elimination System ("NPDES") permit at Citgo's refinery near Lake Charles, Louisiana. On January 29, 1988, Citgo and EPA entered into a Consent Decree under which Citgo agreed to pay a civil penalty of $225,000, implement certain remedial measures, and pay stipulated penalties in the event of violations in the future.

In 1987, Citgo petitioned EPA for variances from certain minimum technological standards established by RCRA as they pertain to certain surface improvements at the Citgo refinery. In January, 1988, EPA granted Citgo variances from the new standards. These variances require Citgo to test surrounding groundwater and to notify EPA if significant increases occur in certain indicator parameters. Citgo believes that it is currently in compliance with the terms of these variances. If the variances are revoked or are otherwise withdrawn, Citgo estimates that the capital improvements which would be required to comply with the referenced standards could exceed $50 million.

On February 21, 1986, the New Jersey Department of Environmental Protection ("NJDEP") issued the Company an Administrative Consent Order relating to groundwater conditions at a chemical manufacturing facility. The Administrative Consent Order required the Company to pay a civil penalty of $50,000 and to conduct a remedial investigation/feasibility study ("RI/FS") at the facility. On August 5, 1987, the Company submitted its initial remedial investigation report to the NJDEP. The Company now expects that the RI/FS and the resulting remedial action will cost at least $10 million.

On August 1, 1987, the Company and NJDEP entered into an Administrative Consent Order pursuant to the New Jersey Environmental Cleanup Responsibility Act ("ECRA") which permitted the Company to comply with the provisions of ECRA after the consummation of the Merger with JT Acquisition. Pursuant to the Order the Company has provided financial assurance in the amount of $4 million and is preparing to implement a cleanup plan for its chemical manufacturing facility in New Jersey.

On February 17, 1987, the Company entered into a Consent Order with the State of Maryland and the City of Frederick, Maryland, concerning wastewater pretreatment at one of the Company's milk processing plants. The Consent Order required the Company to study, design and construct additional pretreatment facilities. Under the Consent Order, as amended, the plant is required to meet the local pretreatment ordinance requirements by January 1, 1989. In July, 1987, at the completion of the design phase of the project, the Company determined that the new wastewater treatment plant required by the Consent Order will cost approximately $3 million.

On May 28, 1985, the United States District Court for the District of New Jersey entered a Consent Decree between the Company and the EPA and two citizen groups, relating to alleged violations of the Company's NPDES permit at a chemical manufacturing facility. The Consent Decree required the Company to pay a civil penalty of $100,000 and to conduct a bioassay testing program and other monitoring. Stipulated civil penalties are provided for failure to comply with the terms of the Consent Decree or failure of the bioassay tests. On July 29, 1987, the Company and the private plaintiffs entered into a settlement agreement regarding attorneys' fees. This settlement effectively concluded this matter.

Citgo is conducting a modernization program involving certain of its products terminal and pipeline facilities which includes updating of equipment required by environmental regulations.

In addition, the Company is installing or improving wastewater pretreatment facilities at several of its food processing and chemical manufacturing plants in order to comply with state and local pretreatment requirements.

In general, the Company's capital expenditures will continue to be affected by federal, state and local environmental laws and regulations. It is possible that future environmental requirements may be more stringent than current requirements, thereby requiring additional expenditures.

Employees

At December 31, 1987, the Company had 65,800 employees, of whom less than two percent were considered to be either temporary or part-time employees, as follows:

	Number of Employees		
Category in which Employed	Regular	Temporary or Part-time	Total
Convenience Retailing	52,350	400	52,750
Food Processing and Manufacturing	1,025	200	1,225
Chief Auto Parts	4,125	25	4,150
Dairies Group	3,275	50	3,325
Distribution Centers	3,100	275	3,375
Corporate	970	5	975
Totals	64,845	955	65,800

The Company has in the past been able to satisfy substantially all of its requirements for managerial personnel from within its organization. Most of the Company's sales and supervisory staff personnel are compensated on some form of incentive basis.

It is estimated that approximately two percent of the Company's regular employees, primarily in the Dairies Group, are subject to collective bargaining agreements. The Company considers its labor relations to be satisfactory.

In addition, Citgo has 3,318 full-time and 162 temporary or part-time employees, approximately 37 percent of whom are subject to collective bargaining agreements.

Item 2. *PROPERTIES.*

Under the Credit Agreement virtually all the Company's assets, not previously subject to liens, were encumbered including both tangible and intangible property rights as well as stock in the Company's non-foreign subsidiaries, where such encumbrance was not otherwise prohibited. In connection therewith, the Company granted a mortgage against its ownership or leasehold interest in approximately 4,300 operating 7-Eleven stores and 100 other properties throughout the United States. The lien (on any real property interests) will be released if the underlying property is sold, the lease to the Company terminates or upon payment by the Company of the amounts due under the Credit Agreement.

CONTINUING OPERATIONS

Convenience Retailing

The 7-Eleven stores group utilizes 322 offices in 37 states and Canada.

The following table shows the location and number of convenience stores (excluding stores under area licenses and of certain affiliates) in operation on December 31, 1987.

State	Operating Convenience Stores		
	Owned	Leased	Total
Alabama	2	22	24
Arizona	50	75	125
Arkansas	5	14	19
California	210	1,078	1,288
Colorado	58	234	292
Connecticut	7	36	43
Delaware	12	24	36
District of Columbia	5	28	33
Florida	297	404	701
Georgia	21	37	58
Hawaii	12	45	57
Idaho	9	14	23
Illinois	60	139	199
Indiana	3	16	19
Iowa	14	17	31
Kansas	8	21	29
Louisiana	39	109	148
Maryland	100	226	326
Massachusetts	11	30	41
Michigan	45	61	106
Minnesota	35	23	58
Mississippi	0	1	1
Missouri	55	100	155
Nevada	63	93	156
New Hampshire	1	7	8
New Jersey	77	142	219
New Mexico	9	38	47
New York	43	167	210
North Carolina	11	54	65
Ohio	14	7	21
Oklahoma	6	14	20
Oregon	39	113	152
Pennsylvania	65	140	205
Rhode Island	0	10	10
South Carolina	6	35	41
Tennessee	26	49	75
Texas	321	755	1,076(b)
Utah	46	125	171
Virginia	197	497	694
Washington	67	247	314
West Virginia	12	3	15
Wisconsin	2	0	2
Canada:			
Alberta	17	113	130
Manitoba	11	46	57
Ontario	31	105	136
British Columbia	23	123	146
Saskatchewan	12	24	36
Total	2,157	5,661	7,818

(a) Of the convenience stores set forth in the foregoing table, 1,325 are leased by the Company from The Southland Employees' Trust (the "Trust"). The Company also leased 82 closed convenience stores, six closed auto parts stores and 21 other locations from the Trust.

(b) On January 21, 1988, the Company completed the sale of its Houston, Texas, convenience store operations to NCS (except one joint-venture location which was not part of the transaction with NCS). The properties sold included 261 convenience stores, nine Quik Marts, four sites for development, 67 closed stores, 29 vacant sites and 19 other properties (including offices and warehouses). This divestiture is not reflected in the above table because it occurred after year-end.

At December 31, 1987, in addition to those properties being sold to NCS in the Houston, Texas, area, there were 109 7-Eleven stores in various stages of construction (21 of which were on property owned by the Company and the others leased), and the Company owned 65, and had leases on 129, undeveloped convenience store sites. Additional purchases and leases were in varying stages of negotiation and in escrow. In addition, the Company held (including those sites in Houston, Texas, which were sold to NCS) 517 7-Eleven, High's and Quik Mart properties for sale consisting of 255 unimproved parcels of land, 158 closed store locations and 104 parcels of excess property adjoining store locations, which, other than the Houston properties, were in addition to the stores being sold as part of the Divestitures.

At year-end 1987, the Company operated 100 Quik Mart stores (nine of which were sold to NCS on January 21, 1988) in Florida, Georgia, Illinois, Indiana, Louisiana, Massachusetts, Missouri, New Hampshire, North Carolina, Texas, Virginia and Wisconsin, 93 of which were owned by the Company and the balance leased.

The Company operates 319 High's Dairy Stores located in Maryland, Virginia, Pennsylvania, West Virginia and the District of Columbia area, 313 of which are on leased property. At December 31, 1987, there were six High's stores under construction and four sites (three of which are owned) held for future development. The Company is currently operating these stores under the High's name. The Company is currently considering the sale or closing of certain of these locations.

As of December 31, 1987, the Company operated 13 Super-7 gasoline stations, 11 in California and two in Washington, which are all owned by the Company, except three that are leased from the Trust.

Generally, the Company's store leases are for primary terms of from 14 to 20 years, with options to renew for additional periods. Many leases contain provisions granting the Company a right of first refusal in the event the lessor decides to sell the property. Many of the Company's store leases, in addition to minimum annual rentals, provide for percentage rentals based upon gross sales in excess of a specified amount and for payment of taxes, insurance and maintenance.

The Company also holds three tracts in Dallas, Texas, not included in Cityplace, totaling about 11 acres, and several other smaller tracts also in Dallas.

The Company owns: (1) a 40-acre tract of land in Orlando, Florida, on which is located a 420,460-square-foot regional distribution center (which includes 40,040 square feet of office space), and an 11,200-square-foot garage facility, including an adjacent 15-acre tract of unimproved land purchased in 1984 for future expansion; (2) a 48-acre tract of land in Tyler, Texas, on which is located a 464,467 square-foot-regional distribution center (which includes 33,051 square feet of office space), a 12,200-square-foot garage facility, which also includes an adjacent 11-acre tract of unimproved land purchased in 1984 for future expansion; (3) a 58.9-acre tract of land in Fredericksburg, Virginia, on which is located a 598,195-square-foot regional distribution center (which includes 37,483 square feet of office space) and a 19,200-square-foot garage facility; (4) an approximately 62-acre tract of land in Champaign, Illinois, on which is located a 543,406-square-foot-regional distribution center (which includes 54,244 square feet of office space) and a 24,080-square-foot garage facility; (5) a 36.74-acre tract of land in San Bernardino, California, on which is located a 293,247-square-foot regional distribution center (which includes 32,680 square feet of office space) and a 12,600 square-foot garage facility; and (6) a five-acre tract of land in Delanco, New Jersey, on which is located a 19,000-square-foot branch distribution facility. In addition, the Company leases four separate facilities used as relay stations for the distribution centers in Florida, Virginia and Texas. During 1987, approximately 27 acres of the land in Champaign, Illinois, were sold.

The Company owns four food processing facilities which are located at the Company's regional distribution centers: (1) a 13,000-square-foot food processing facility in Orlando, Florida; (2) a 40,000-square-foot food processing center in Tyler, Texas; (3) a 49,200-square-foot food processing center in Fredericksburg, Virginia; and (4) a 45,568-square-foot food processing center in Champaign, Illinois, which contains a 3,300-square-foot batch-cooking operation which opened in April 1986. In addition, the Company owns a 21.5-acre tract of land in Salt Lake City, Utah, on which is

located an 80,000-square-foot food processing plant (which includes 6,930 square feet of office space) and a 25,100-square-foot food processing center in St. Louis, Missouri, which includes office space leased to a third party. The Company also owns a parcel of land and freezer facility in Odessa, Texas, which is available for resale.

In connection with its acquisition of Rainbow Ticketmaster, Inc., the Company leases office facilities in Dallas, Houston and San Antonio, Texas, and Phoenix, Arizona, and has a concessions agreement for space in an entertainment arena in El Paso, Texas.

Svenska/7-Eleven AB owns two and leases 66 store locations and leases four offices in Sweden.

Citgo Petroleum Corporation

The Refinery is located on approximately 2,500 acres owned by Citgo on the west bank of the Calcasieu River near Lake Charles, Louisiana. Of the approximately 4,000 acres of additional land owned by Citgo in Calcasieu Parish, Louisiana, 2,500 acres are currently leased for grazing or farming purposes.

Citgo's product distribution system includes 42 wholly or partially owned products terminals with a total tankage capacity of approximately 18 million barrels. These facilities, which are located in Alabama, Florida, Georgia, Illinois, Indiana, Louisiana, Massachusetts, Michigan, New Jersey, New York, North Carolina, South Carolina, Tennessee, Texas, Virginia, and Wisconsin can receive product via trucks, pipelines and marine vessels. Seven other terminals are used for product inventory, and over 300 additional terminals are used under exchange agreements with other wholesalers. Fourteen additional tracts in Texas, six of which are approximately 10 acres each, one 49.3 acres, one approximately 15 acres, and six between one and eight acres each, are used as gasoline storage facilities or truck terminals. To facilitate delivery of products to its customers, Citgo, through a wholly owned subsidiary, Petro-Chemical Transport, Inc., owns or leases a fleet of 100 tractors and 123 trailers. Citgo also owns 25 aircraft refuelers and owns or leases approximately 280 rail cars which currently fulfill all other surface transportation requirements.

In addition, Citgo has a crude oil dock facility and a crude oil tank farm, both located near the Refinery, consisting of approximately four million barrels of tankage, and tanker and barge docks on the Calcasieu Ship Channel. A portion of the terminal is for heavy fuel, consisting of 320,000 barrels of insulated tankage.

Citgo owns and operates a 1,300-mile common carrier crude oil pipeline system located primarily in Texas and Louisiana and has joint equity interests in three common carrier crude oil pipelines with a total of approximately 6,000 miles of pipeline and six refined product pipelines with total mileage of approximately 8,000 miles.

Citgo's crude oil trunkline interests are supported by the Sour Lake Tank Farm, which has 22 tanks with over two million barrels of storage capacity and receives crude oil from West Texas Gulf Pipe Line Company, the East Texas Main Line System, Koch Pipeline Company, Sun Pipeline Company, Citgo Pipeline Company's Fauna-to-Sour Lake 12-inch line and Mobil Pipeline Company. Citgo owns additional storage facilities with 720,000 barrels of capacity (Fauna Storage Facility), and additional support facilities in Texas and Louisiana. Additional properties (21 owned, 47 leased) in Arkansas, Kansas, Louisiana, New Mexico, Oklahoma and Texas are used as tank farms, pump stations, booster stations, gathering stations and similar functions.

Citgo also owns a compounding plant in Cicero, Illinois, a jet fuel facility at Miami International Airport and various offices, excess parcels and other properties, most of which are located adjacent to terminals.

Twenty-three Citgo service stations are operated by dealers (four owned and 19 leased). In addition, Citgo owns and operates 14 Quik Marts in Oklahoma.

Citgo's corporate and administrative personnel occupy 257,599 square feet of leased office space in Tulsa, Oklahoma, and 21,000 square feet of leased office space in Carrollton, Texas. Citgo also leases a total of 26,250 square feet of space for storage/warehouse purposes at a separate location in Tulsa.

Corporate

The Company's corporate office is in Dallas, Texas, where it occupies approximately 655,000 square feet in 17 buildings, including an 11-story tower which contains approximately 132,000 square feet of office space. The 11-story tower, and the East Tower which will house the Company's new corporate headquarters, are located on a 160-acre tract which was acquired by the Company for development as Cityplace, a multi-use development. The Company now intends to explore various alternatives for the development of the Cityplace land that is not being used for the East Tower, including sales of joint venture interests and land sales. The 42-story East Tower, parking garage and related space, are currently nearing completion, (see "Cityplace," page 11). The Company also utilizes other office space in and around Dallas.

The Company has a long-term sublease on 18 acres at Love Field, Dallas (see "Citijet," page 11), on which are located 10 acres of ramp space, three airplane hangars of approximately 154,000 square feet, a terminal building of 19,400 square feet and a three-story office building containing 34,000 square feet which has been leased to a third party.

OPERATIONS BEING DIVESTED

Food Processing and Manufacturing

The following table sets forth the production facilities of the Dairies Group by state. All facilities listed are intended to be divested as part of the Divestitures. The number, capacity and percentage of utilization of the Dairies Group processing plants at December 31, 1987, was as follows:

State	Number of Food Processing Plants Owned	Number of Food Processing Plants Leased	Fluid Products Capacity Gal/Year	% Capacity Utilized	Frozen Products Capacity Gal/Year	% Capacity Utilized
California	4	—	40,495,000	100.77%	—	—
Colorado	—	1	3,120,000	89.68%	—	—
Florida	2	—	28,340,000	104.20%	5,720,000	38.30%
Maryland	2	—	14,560,000	160.55%	5,200,000	77.10%
Missouri	1	—	—	—	4,160,000	134.48%
Texas	8	—	71,635,200	93.47%	12,667,200	42.40%
Washington	1	—	—	—	1,587,040	90.49%
Wisconsin	1	—	3,120,000	132.61%	—	—
Total	19	1	161,270,200	103.93%	29,334,240	63.41%

(a) Fluid and frozen production is based on the maximum production in one eight-hour shift, five days per week, 52 weeks per year.

The dairies process cultured products at four of the plants included in the above table: one in California, two in Texas, and one in Wisconsin.

The dairies' facilities also include an owned ice facility and dry and cold storage operation in Missouri and a leased plastic bottle manufacturing plant in Texas, as well as a leased hard cheese cutting and wrapping facility in Wisconsin. None of these is included in the above schedule. In addition, the table does not include a milk processing plant and an ice cream manufacturing plant connected with the High's Dairy operation.

Dairy product distribution points are located at each processing plant and at 34 separately owned or leased locations.

During 1987 the Dairies Group acquired (a) land adjacent to its Winter Haven, Florida plant (for expansion); (b) land near its Baltimore, Maryland plant (for parking); (c) land near its South Gate, California plant (for parking and garage); and (d) land, office, vault and garage space in San Leandro, California, which was formerly leased from a third party. In addition, the Dairies Group sold (a) its French's Ice Cream plant in Atlanta, Georgia; (b) the Embassy Dairy ice cream distribution facility in Fairfax, Virginia; and (c) land in Torrance, California, and closed (a) its juice plant in Watsonville, California; (b) its ice cream plant in Memphis, Tennessee, which is currently for sale by the Dairies Group; and (c) its ice cream plant in Alexandria, Virginia, which is available for sublease.

The Chemical/Food Labs operations utilize one plant facility each in Illinois, New Jersey and Texas and a separate office in Illinois, all of which are owned by the Company.

The Tidel Systems Division leases an office, warehouse and manufacturing facility and a sales office in Texas.

As of December 31, 1987, the Company owned eight ice manufacturing plants, six in Texas and one each in Florida and Nevada. In March 1987, the Company sold its ice manufacturing plant in Oklahoma. Reddy Ice also leases warehouse facilities in Texas and Utah which are used for storage and supplies.

The Company also owns a corn chip manufacturing facility in South Beloit, Illinois, containing approximately 94,000 square feet, including office space. In addition, the Company holds one vacant parcel of land in South Beloit that is available for sale.

The Company owns a leasehold interest in a potato chip manufacturing and distribution plant in York, Pennsylvania, consisting of approximately 4.1 acres of land and four attached buildings with a total of 133,175 square feet of floor area along with an additional 5,280 square feet of basement area.

The Company also owns a pretzel manufacturing facility in Lititz, Pennsylvania, of about 45,000 square feet, including office space, on approximately 8.6 acres of land, including 3.6 acres which are vacant.

Chief Auto Parts

As of December 31, 1987, Chief Auto Parts had 469 operating stores located in Alabama, Arizona, Arkansas, California, Kentucky, Nevada, Oklahoma, Tennessee and Texas, 113 of which are owned by the Company and the balance leased (47 from the Trust); one leased distribution center (in California containing approximately 150,180 square feet with an annex of 46,080 square feet). The Company also owns a 250,000-square foot warehouse facility in Seagoville, Texas, which was placed in operation as a new Chief distribution center in early 1987, and leases 10 offices and two office/warehouse facilities in California and Texas. At December 31, 1987, 14 Chief Auto Parts stores were under construction (3 on property owned by the Company and the balance leased), and 17 additional sites were approved but not yet started (13 on Company property and 4 leased). The Company is selling or conveying all of the operating stores, the distribution center, the warehouse facility, a tract of land adjacent to the warehouse facility and certain other related properties as part of the Divestitures.

Item 3. *LEGAL PROCEEDINGS.*

Two complaints which purport to be class actions on behalf of all persons who sold stock of the Company during certain time periods in 1987 prior to the Tender by JT Acquisition were filed against various parties in the United States District Court, Northern District of Texas. These actions were subsequently consolidated. The first consolidated class action complaint (the "Complaint") alleges that the defendants violated federal securities laws and state law by failing to timely and accurately disclose certain expressions of interest by third parties in acquiring Southland, as well as the Thompsons' own steps to seek to acquire Southland. The Complaint seeks punitive damages of at least $100,000,000 and

compensatory damages in an unspecified amount. In September 1987, a third complaint, alleging similar claims, was filed with the United States District Court, Eastern District of New York. This complaint is in the process of being transferred to the Northern District of Texas. A fourth complaint, alleging similar claims, was filed with the United States District Court, Northern District of Texas in December 1987. The defendants believe the complaints to be without merit and intend to defend vigorously against them. The Securities and Exchange Commission has issued a private order of investigation concerning the trading of Southland stock during various times in 1987 and the issuance of various public statements by Southland.

In addition, as previously reported in a Form 8-K dated February 16, 1988, the Company's Velda Farms Dairy Division has been named as one of the defendants in a suit filed by the Florida Attorney General's office in connection with alleged abuses in bidding practices in school milk contracts in that state.

Information concerning other legal proceedings is incorporated herein from "Environmental Matters," pages 15 through 17, above.

Item 4. *SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.*

A Special Meeting of Shareholders was held on December 8, 1987, to vote upon a proposal to approve an Agreement and Plan of Merger, dated as of July 3, 1987, as amended, between the Company and JT Acquisition Corporation, pursuant to which JT Acquisition Corporation was merged with and into the Company and the directors of JT Acquisition Corporation at the time of the merger (Messrs. John P. Thompson, Jere W. Thompson and Joe C. Thompson, Jr.) would become the directors of the Company.

At the meeting 43,042,140 shares of Common Stock and 2,419,949 shares of $4.00 Cumulative Convertible Exchangeable Preferred Stock, Series A (the "Preferred Stock, Series A") voted for the proposal, 17,836 shares of Common Stock and 200 shares of Preferred Stock voted against the proposal and 15,865 shares of Common Stock abstained from voting.

PART II

Item 5. *MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.*

The Company's common stock, $.01 par value per share, is the only class of common equity of the Company and represents the only voting securities of the Company. There are 200,000,000 shares of common stock outstanding. The Company's common stock was listed and traded on the New York Stock Exchange, Inc. and the Pacific Stock Exchange, Inc. until December 15, 1987, the date of the Merger. The common stock is not now publicly traded and there are currently four holders of the common stock. (See Item 12, Securities Ownership of Certain Beneficial Owners and Management).

The following table provides the high and low sales prices for the common stock and the cash dividends paid thereon for each quarter during the two most recent fiscal years:

	Price Range		Cash
	High	Low	Dividends
1987:			
First quarter	$54⅞	$44	$.28
Second quarter	69½	44	.28
Third quarter	80¼	66½	—
October 1 through December 15	74½	44	—
1986:			
First quarter	$50	$40⅜	$.28
Second quarter	56⅜	44⅞	.28
Third quarter	56⅞	45¼	.28
Fourth quarter	60½	45⅛	.28

Item 6. *SELECTED FINANCIAL DATA.*

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

SELECTED FINANCIAL DATA

The financial data for the five months ended December 31, 1987, reflects the purchase of the Company by JT Acquisition Corporation, and a resultant new basis of accounting. The figures for the five months are not comparable to those for any prior period. See Note 1 of Notes to the Consolidated Financial Statements.

	Successor	Predecessor				
	Five months ended December 31, 1987	Seven months ended July 31, 1987	Year Ended December 31 1986	1985	1984	1983
	(Dollars in millions, except per-share data)					
Net sales	$3,211.0	$4,865.4	$7,782.7	$7,856.7	$7,389.4	$6,648.0
Other income	14.6	33.9	40.3	43.5	41.6	21.2
Total revenues	3,225.6	4,899.3	7,823.0	7,900.2	7,431.0	6,669.2
Earnings (loss) before business units to be divested	(149.7)	74.9	178.6	196.5	144.8	119.5
Net earnings (loss)	(149.7)	90.1	200.4	212.5	160.3	131.8
Earnings (loss) before business units to be divested per common share						
Primary	(0.75)	1.42	3.51	4.07	3.08	2.96
Fully diluted	(0.75)	1.42	3.49	4.04	3.05	2.92
Net earnings (loss) applicable to common shares						
Primary	(0.75)	1.74	3.96	4.41	3.41	3.26
Fully diluted	(0.75)	1.74	3.91	4.37	3.38	3.21
Total assets	5,382.2	N/A	3,300.4	3,131.2	2,465.4	2,172.0
Long-term debt	3,978.9	N/A	622.7	564.2	557.3	534.3
Redeemable preferred stock	91.3	—	—	—	—	—
Cash dividends per common share	0.56	0.56	1.12	1.00	0.92	0.84

Item 7. *MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.*

Financial Review for 1987

On July 3, 1987, the Board of Directors of Southland unanimously approved an Agreement and Plan of Merger (Merger Agreement) with JT Acquisition Corporation (JT Acquisition), an affiliate of The Thompson Company, the investment firm of the founding family of Southland. The Merger Agreement provided for the acquisition of Southland in a two-step leveraged buyout (LBO) transaction. The first-step tender offer was successfully completed on August 1, 1987. At that time JT Acquisition accepted for payment 31.5 million shares of the Company's common stock at $77 per share in cash and 2.42 million shares of the Company's $4.00 Cumulative Convertible Exchangeable Preferred Stock, Series A (the Preferred Stock Series A) at $90.27 per share in cash. The shareholders approved the merger on December 8 and the merger of Southland and JT Acquisition was consummated on December 15, 1987 (the Merger). In the Merger, each outstanding share of Southland common stock was converted into $61.32 in cash and 0.6672 of a share of a new class of preferred stock, the 15% Cumulative Exchangeable Preferred Stock, Series One (Redeemable Preferred). Each remaining outstanding share of Preferred Stock Series A was cancelled and exchanged for $90.27 in cash.

In the future, the Company intends to concentrate its efforts on its convenience retailing operations. Southland will divest substantially all other business units and approximately 1,000 operating convenience stores. Southland will retain the Distribution Centers, Food Centers and its half-interest in Citgo. Agreements have been reached for the sale of the Dairies, Chief Auto Parts, Tidel Systems and Reddy Ice divisions as well as 473 operating 7-Eleven stores in ten states. It is anticipated that these transactions will be completed by the end of April 1988. In March 1988, the Company's Japanese yen royalty stream was monetized. The Company also completed the sale of an additional 270 operating convenience stores in the Houston area and the sale of its MovieQuik videocassette rental division in the early part of 1988. In addition the Company will sell its Chemical and Snack Food Divisions and certain other assets including approximately 250 other operating stores. (See Notes 8 and 9 to the Consolidated Financial Statements for discussion of the accounting treatment of these Divestitures.)

Balance Sheet

The Merger was recorded under the purchase method of accounting. Accordingly, the purchase price has been allocated to the assets of the Company based on their fair market values. Consequently the December 31, 1987, balance sheet reflects the new basis of accounting for these assets. The excess of the purchase price over the fair value of Southland's net assets, which totaled $931 million (net of amortization), is reflected on the December 31, 1987, balance sheet.

The recapitalization of the Company resulting from the LBO is also reflected on the balance sheet. The common stock outstanding prior to the Merger was exchanged for cash and Redeemable Preferred. The outstanding Preferred Stock Series A was exchanged for cash. In the Merger, the shareholders of JT Acquisition were issued 200 million shares of common stock, $.01 par value. Shareholders' equity has been adjusted to reflect the total share of the Company owned by the Thompsons valued at their proportionate share of the historical book value of the Company reduced by the consideration paid for the shares not retained by JT Acquisition.

The balance sheet also reflects the addition of $4 billion of new debt to facilitate the Merger and the redemption of about $114 million of certain publicly held debentures.

Financing Activities

The Company has incurred significant levels of new debt to finance the LBO. Upon consummation of the Merger, the Company became obligated for $2.5 billion of bank debt under the terms of a Credit Agreement. The Credit Agreement includes three separate loan facilities: the Revolving Credit Facility, the Senior Term Loan and the Divestiture Term Loan. The Credit Agreement contains numerous financial and operating covenants. These covenants include, but are not limited to, requirements that the Company maintain certain financial ratios and restrict the Company's ability to pay cash dividends on the Redeemable Preferred, to make certain investments (including capital expenditures), to incur indebtedness and to sell assets.

The Revolving Credit Facility is to fund the Company's operating requirements and cannot exceed $450 million in the aggregate at any one time. This facility expires on December 31, 1992. The

Revolving Credit Facility will be reduced to $400 million on December 31, 1990 and further reduced to $350 million on December 31, 1991. The Senior Term Loan is for $2 billion and must be repaid by December 31, 1995. Repayment of the loan is scheduled through installments of $300 million on both December 31, 1988, and December 31, 1989, and quarterly installments ranging from $37.5 million to $75 million commencing March 31, 1990 through December 31, 1995. The Divestiture Term Loan is payable in installments of $45 million on December 31, 1988, $175 million on June 30, 1989, and $275 million on December 31, 1989. Proceeds from the sale of certain business units and other assets will be used to prepay the installments of the Divestiture Term Loan and the Senior Term Loan.

Interest on the Revolving Credit Facility, the Senior Term Loan and the Divestiture Term Loan is payable quarterly at a variable rate equal to the lead bank's prime rate plus 1.5% per year, or, at the Company's option, at a rate equal to the reserve-adjusted Eurodollar rate plus 2.5% per year.

Under terms of the Credit Agreement, the Company is required to maintain interest rate contracts by which it is protected against increases in short term interest rates for 50% of the then outstanding amount of the term loans within one year. By early 1988, the Company had entered into agreements with maturities of two to four years that fix the interest rate at an average of 9.1% on $515 million of debt. Additionally, Southland entered into one- to four-year agreements which provide reimbursement to the Company to cover incremental interest costs on $315 million of debt if the three-month LIBOR exceeds 9% and on $50 million if this rate exceeds 9.5%.

The Company has also issued four series of debentures and notes for $1.5 billion to complete the financing for the Merger. This financing consisted of $350 million of Senior Subordinated Notes (the Notes); $402 million of Senior Subordinated Discount Notes (the Discount Notes); $500 million of Subordinated Debentures (the Debentures); and 946,945 Units consisting of an aggregate of $947 million of Junior Subordinated Discount Debentures (the Discount Debentures) and 26.1 million Warrants to purchase common stock (the Warrants).

The Notes bear interest at 15¾% with semiannual interest payments commencing June 15, 1988. The Notes provide for a sinking fund payment equal to one-half of the principal outstanding on December 15, 1996, and are to be paid in full by December 15, 1997. These Notes are redeemable at the Company's option from December 1992 through December 1993 at 105% of principal, from December 1993 through December 1994 at 102.5% of principal, and thereafter until maturity at 100% of principal.

The 16½% Discount Notes were issued at a discount of $152.3 million from their principal amount. The discount will be accreted through December 15, 1990. Thereafter the Discount Notes require semiannual interest payments beginning June 15, 1991. They are redeemable at the Company's option at any time, in whole or in part, at 100% of principal until their maturity at December 15, 1997.

The Debentures carry an interest rate of 16¾% with semiannual interest payments beginning June 15, 1988. The Debentures require sinking fund payments equal to 20% of the principal outstanding on December 15 each year commencing in 1998. They are redeemable at the Company's option at amounts ranging from 106% of principal beginning December 1992 to 101½% at December 1995. Beginning December 1996, they may be redeemed at 100% of principal until maturity at December 15, 2002.

The 18% Discount Debentures were issued at a discount of $573 million. The discount will be accreted through December 15, 1992. Semiannual interest payments commence June 15, 1993. The Discount Debentures require sinking fund payments on December 15, 2003 through 2007, each for 20% of the principal outstanding. The Discount Debentures are redeemable at the Company's option at any time at 100% of principal until maturity at December 15, 2007.

The Warrants which were issued with the Discount Debentures represent the right to purchase approximately 10% of the Company's common stock at an exercise price of $1.00 per share in certain circumstances or entitle the holder to other rights in lieu of the purchase of stock. The Warrants

may be exercised prior to December 16, 1992 if the Company has a public offering of common stock or is involved in certain business combinations. Otherwise, the Company is obligated to repurchase all outstanding warrants by March 15, 1995, for cash or subordinated debt. The repurchase price will be the fair market value of the Warrants as determined by an independent financial expert.

The Redeemable Preferred, which was issued in exchange for common stock outstanding at the Merger date, has a stated value and liquidation preference of $25 per share. The Redeemable Preferred pays cumulative quarterly dividends at the annual rate of $3.75 per share, payable when and if declared by the Company's Board of Directors out of funds legally available. During the first 20 quarters following the Merger, the Company has the option to pay dividends in either cash or additional shares of Redeemable Preferred. The Redeemable Preferred may be redeemed at the Company's option, in whole or in part, at any time prior to December 15, 1989, at $25.75 per share and at any time thereafter at $25.00 per share plus accrued but unpaid dividends. The Company is required to redeem at least 10% of the Redeemable Preferred each year from 1998 through 2007. The Redeemable Preferred is exchangeable at the option of the Company after December 15, 1989, into debentures which will have an interest rate of 15%. This interest may be paid in additional debt securities. The debentures would be due in 2007 and would require sinking fund payments from 1998 through 2007 equal to 10% of the principal outstanding as of December 15, 1992.

Fees of approximately $200 million were incurred in conjunction with the LBO. Of this amount $194 million was capitalized and will be amortized either over the life of the corresponding debt instruments or through goodwill amortization. The remaining amount was expensed in 1987.

In conjunction with the Merger, the Company redeemed its 8⅜% Sinking Fund Debentures due 2002, its 9⅜% Sinking Fund Debentures due 2003 and its 9½% Sinking Fund Debentures due 2004 with principal in aggregate of $113.7 million.

In March 1988, the Company announced a financing agreement for 41 billion yen at an estimated exchange rate of 126 yen per dollar, or approximately $325 million. This financing enables the Company to monetize its future yen royalty stream and to apply $300 million of the proceeds toward repayment of the debt incurred in the LBO. Payments of principal and interest on the yen-denominated debt, which is nonrecourse to Southland, will be made from future yen royalties. The financing is collateralized by the Company's Japanese 7-Eleven trademarks and the right to receive royalties from Seven-Eleven Japan Co., Ltd., the Company's licensee in Japan.

In early 1987, Cityplace Center East Corporation, a subsidiary of the Company, issued $290 million of 7.875% notes in connection with the construction of the Company's new headquarters building. Interest payments are semiannual with the principal due February 1995. The notes are nonrecourse to Southland.

Sources of Funds

The most significant sources and uses of funds during 1987 were the transactions relating to the LBO which have been discussed above.

Funds from Southland's continuing operations have historically produced high levels of cash flow to fund capital expenditures. For the year ended December 31, 1987, $322 million was provided from operations which funded 56% of the capital expenditures during that period. The Company's capital spending activities were significantly curtailed following the announcement of the LBO.

Funds provided by the $290 million notes issued in March 1987 by Cityplace Center East Corporation were used to retire commercial paper which had served as interim financing for the project with the balance applied to remaining construction costs.

Another source of funds in 1987 was the repayment of $100 million by Citgo of a previous advance made by Southland to this affiliate.

Additional funds were provided by borrowings from commercial paper and short-term credit facilities. Following the LBO, the commercial paper market is no longer available to the Company and its short-term borrowings under the Revolving Credit Facility are regulated by terms of the Credit Agreement.

In the past, capital and operating leases have been important alternatives available to the Company for new store development. Under terms of the Credit Agreement, the Company's ability to enter into new lease arrangements will also be limited.

Uses of Funds

During 1987, the Company invested $574 million in capital expenditures. Of this amount, $158 million was for Cityplace related expenditures. Construction costs for Cityplace in 1988 are estimated to be approximately $100 million. Under terms of the Credit Agreement future capital expenditures cannot exceed $167 million, $62 million and $145 million in 1988, 1989, and 1990, respectively. The Company believes these amounts will be sufficient to maintain its facilities and provide needed capital to meet competitive requirements.

Additional uses of funds during 1987 were $7.6 million in dividends paid on Preferred Stock Series A and $27.1 million in dividends paid on common stock outstanding prior to the Merger.

In the future, the Company's high level of debt will require that a large portion of internally generated funds be used for interest payments and debt retirement.

Income Taxes

Although the Company expects improved profitability from operations, it is anticipated that net losses will be generated over the next several years due primarily to the interest expense associated with the high debt levels. As a result, the Company does not anticipate that it will be a tax paying entity and will use a portion of these losses as carrybacks to recover taxes paid in previous years.

MANAGEMENT'S REVIEW OF OPERATING RESULTS — FIVE MONTHS ENDED DECEMBER 31, 1987 AND SEVEN MONTHS ENDED JULY 31, 1987.

Five Months Ended December 31, 1987

Net sales were $3.2 billion. Convenience store sales accounted for $3.0 billion or 94.7% of the Company's total sales. Merchandise sales in convenience stores were $2.4 billion while gasoline sales were $0.6 billion. Real growth after inflation in stores open more than one year (including the 1,000 convenience stores scheduled for future divestiture) was a negative 0.58% during this period, despite improved profitability.

The Company's consolidated gross margin was 23.3%. Merchandise gross margins improved compared to the five months of 1986 due primarily to the stores' more targeted merchandising efforts and the benefits derived from the Company's previous investment in new marketing programs. Gross profit per gallon of gasoline during the last five months of 1987 was 10.7 cents. The unusually strong gasoline profits reflect industry conditions and certain strategic adjustments that focus on further improving profitability from the Company's gasoline marketing operations.

The ratio of expenses (selling, general and administrative, interest, contributions to profit sharing plan) to sales was 31.1%. The large increase in this ratio is primarily attributed to significantly higher interest costs which includes amortization of deferred debt issuance costs associated with the Company's new debt levels. Certain other nonrecurring expenses including the cost to redeem all outstanding stock options, fees related to the financing of the tender offer and the loss associated with the unhedging of currency exchange agreements resulting from the monetization of the Japanese yen royalties contributed to the increase of this ratio.

The Company's net earnings for the period include $14.2 million from its 50% equity in Citgo's net earnings.

A tax benefit of $71.8 million was recorded by the Company during the last five months reflecting its loss position resulting from higher interest expense and other costs related to the LBO.

Seven Months Ended July 31, 1987

Net sales for the period were $4.9 billion. Convenience store sales accounted for $4.6 billion or 95.2% of total sales. Merchandise sales in convenience stores were $3.6 billion while gasoline sales were $1.0 billion. Real growth after inflation in stores open more than one year was 2.26%.

The Company's consolidated gross margin was 20.8%. Merchandise gross margins declined slightly compared to the seven months of 1986 primarily due to the stores' continued competitive pricing strategy in certain markets. Gross profit per gallon of gasoline was 7.5 cents. The ratio of expenses (selling, general and administrative, interest, contributions to profit sharing plan) to sales was 20.6%.

Other income during the period was $33.9 million; primarily consisting of interest income, gains from the sale of assets no longer used in the business and area license royalties.

The Company's net earnings for the period include $39.1 million from its 50% equity in Citgo's net earnings. In addition, during the early part of 1987 the remaining portion of the deferred capital gain of $23.3 million from the sale of a half-interest in Citgo to a subsidiary of Petroleos de Venezuela, S.A. (PDVSA) was recognized. This amount would have been repayable to PDVSA if market prices of petroleum products had not increased sufficiently. Also included in the Company's net earnings for the period is $15.2 million representing the net earnings from the business units to be divested.

Income tax expense for the period was $42.9 million (including the amount allocated to the units to be divested) reflecting the Company's expected overall effective tax rate for the period of 32.2%.

MANAGEMENT'S REVIEW OF OPERATING RESULTS FOR 1986 AND 1985

The following discussion pertains to the Company's operating results for 1986 and 1985 only. No comparison is made to 1987 in this section.

Revenues

Convenience store revenues (net sales of products and services, including sales by 7-Eleven stores operated by franchisees, and other income), which comprise substantially all of the Company's revenues declined slightly in 1986 due to the sharp decline in retail gasoline prices.

Merchandise sales accounted for 76.7% of the convenience stores' sales in 1986, compared to 70.7% in 1985.

	1986	% Change	1985	% Change
Sales (millions)	$5,668.1	7.7	$5,264.7	8.7
Number of stores	8,181 *	5.7	7,743	(0.6)

* Number includes 346 High's Dairy Stores, of which 83 sold gasoline. Because these stores were not acquired until December 30, 1986, their sales and operating results are not included.

More efficient use of selling space, increased advertising, new products and services, and traffic building competitive pricing of selected items such as milk, beer, carton cigarettes and soft drinks, contributed to the increase in merchandise sales and resulted in real growth of 3.7% in 1986 and 4.3% in 1985 in stores open more than one year. The net addition of 153 and 46 7-Eleven stores in 1986 and 1985 also contributed to the sales increase.

Self-serve gasoline, the largest single product category in the convenience stores' sales mix, was 23.3% of 1986 sales, compared to 29.3% in 1985.

Gasoline sales declined in 1986, despite increases in both the number of stores selling gasoline and the average gallonage sold per store, due to the decrease in retail gasoline prices.

	1986	% Change	1985	% Change
Sales (millions)	$1,720.1	(21.2)	$2,183.3	23.8
Gallons (millions)	2,048.8	4.3	1,965.2	22.2
Gross profit (millions)	$ 193.2	29.9	$ 148.7	30.0
Gross profit per gallon (cents)	9.4	24.6	7.6	6.5
Number of stores	3,594 *	4.2	3,449	(2.2)

*See footnote to previous table.

Other income declined slightly in 1986, despite increases in interest income and area license royalties, as gains from the sale of assets no longer used in the business decreased. In 1985, other income remained relatively flat as gains from the sale of assets were offset by less gains from the repurchase of debentures to meet sinking fund requirements.

Gross Profits and Margins

Gross profits (sales less cost of goods sold) were up 6.7% and 5.8% while sales were flat in 1986 and increased 6.3% in 1985. The impact of inflation was not significant on Southland's gross profits these two years due to the low rates of inflation. For the periods, gross margins (gross profits divided by sales) were 21.98 and 20.40.

Gross margins increased in 1986 due to significantly higher gasoline margins and an improved performance from the distribution operations.

The overall convenience stores' gross margin increased in 1986 due to the higher gasoline margins that more than offset a decline in merchandise margins. The decline in merchandise margins resulted from the continuing economic recession in many southern and mid-western markets that depend heavily upon the depressed energy, construction and agricultural industries. In addition, the competitive pricing strategy in certain markets contributed to the decline. In 1985, the convenience stores' gross margin declined due to lower merchandise margins, which resulted primarily from more aggressive promotional programs in divisions serving Houston and other Gulf Coast areas.

Selling, General and Administrative Expenses

In 1986 and 1985, selling, general and administrative expenses increased 7.6% and 8.2%. The ratios of these expenses to sales were 19.68 and 18.12, respectively.

Lower sales, resulting from the decline in retail gasoline prices, and higher expenses caused selling, general and administrative expenses as a percent of sales to increase 1.56 percentage points to 19.68% in 1986. The financing costs associated with the sale of accounts receivable and increased insurance expenses caused the ratio of these expenses to sales to increase in 1985.

Interest and Imputed Interest Expense

Interest expense in 1986 remained at 1985 levels, because lower interest rates and increases in capitalized interest offset the effects of higher average debt levels. Imputed interest expense increased 3.0% in 1986, following a decline of 2.8% in 1985, reflecting increased use of capital leases.

Equity in Earnings of Citgo

Equity in earnings (loss) of Citgo declined $164.7 million in 1986. The negative comparison with 1985 was due to a net $112 million pretax non-cash inventory charge recorded by Citgo in 1986 and

a decline in operating earnings resulting from poor results in the first quarter. In 1985 equity in earnings of Citgo increased $138.5 million. The fluctuations in Citgo's earnings during these years were the result of the prevailing conditions in the petroleum refining and marketing industry.

Income Taxes

The overall effective income tax rates for Southland, including business units to be divested, were 18.5% in 1986 and 24.7% in 1985. These rates were below the federal statutory rate of 46% primarily due to tax benefits arising from Citgo. The reduction in the effective rate in 1986 was attributed to Citgo's loss and the reduced tax rate on the $114.7 million capital gain realized from the sale of half of Citgo.

Net Earnings

Earnings increased 1.6% in 1986 before income taxes, the net effect of Citgo, and earnings of business units to be divested. However, equity in the loss of Citgo was only partially offset by the gain on the sale of half of Citgo and lower income taxes, which resulted in net earnings declining $12.1 million or 5.7% in 1986. Citgo's improved performance contributed to increased earnings in 1985.

Item 8. ***FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.***

INDEPENDENT AUDITORS' REPORT

Board of Directors and Shareholders
The Southland Corporation
Dallas, Texas

We have examined the consolidated balance sheets of The Southland Corporation (wholly owned by affiliates of The Thompson Company) and subsidiaries (the Successor subsequent to the merger with JT Acquisition Corporation) as of December 31, 1987, and the related consolidated statements of operations, shareholders' equity and changes in financial position from August 1, 1987 (inception) to December 31, 1987. We have also examined the consolidated balance sheet of The Southland Corporation and subsidiaries (the Predecessor prior to the merger with JT Acquisition Corporation) as of December 31, 1986, and the related consolidated statements of operations, shareholders' equity and changes in financial position for the seven-month period ended July 31, 1987, and for the years ended December 31, 1986 and 1985. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of The Southland Corporation and subsidiaries (Successor and Predecessor, respectively) at December 31, 1987 and 1986, and the results of their operations and the changes in their financial position for the five-month period ended December 31, 1987, the seven-month period ended July 31, 1987, and the years ended December 31, 1986 and 1985, in conformity with generally accepted accounting principles which, as to the financial statements relating to the Predecessor, have been applied on a consistent basis.

Touche Ross & Co.
Certified Public Accountants

Dallas, Texas
March 23, 1988

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except per-share data)

ASSETS

	December 31	
	1987 (Successor)	1986 (Predecessor)
CURRENT ASSETS:		
Cash and short-term investments	$ 16,090	$ 71,197
Accounts and notes receivable	152,010	112,476
Inventories	307,370	328,847
Deposits and prepaid expenses	24,752	43,877
Investment in properties	—	24,400
Business units to be divested	353,101	323,552
Other assets held for sale	283,815	—
TOTAL CURRENT ASSETS	1,137,138	904,349
PROPERTY, PLANT AND EQUIPMENT	2,344,449	2,019,871
INVESTMENT IN AND ADVANCES TO CITGO	380,037	286,584
EXCESS OF COST OVER FAIR VALUE OF NET ASSETS ACQUIRED IN MERGER	931,309	—
OTHER ASSETS	589,220	89,643
	$5,382,153	$3,300,447

LIABILITIES AND SHAREHOLDERS' EQUITY

	1987 (Successor)	1986 (Predecessor)
CURRENT LIABILITIES:		
Commercial paper and notes payable to banks	$ —	$ 215,291
Accounts payable and accrued expenses	645,862	539,840
Accounts payable to related parties	59,474	53,318
Income taxes	589	23,975
Long-term debt due within one year (including $3,185 and $3,128 due to related parties)	627,344	25,761
TOTAL CURRENT LIABILITIES	1,333,269	858,185
DEFERRED CREDITS AND OTHER LIABILITIES	102,969	151,740
LONG-TERM DEBT (including $30,262 and $34,798 due to related parties)	3,978,902	622,691
REDEEMABLE PREFERRED STOCK, 15% Cumulative Exchangeable Preferred Stock, Series One	91,288	—
COMMON STOCK PURCHASE WARRANTS	26,136	—
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS' EQUITY (DEFICIT):		
Successor:		
Common stock, $.01 par value; 300,000,000 shares authorized, 200,000,000 shares issued and outstanding	2,000	—
Additional capital	14,587	—
Accumulated deficit	(166,998)	—
Predecessor:		
Cumulative Convertible Exchangeable Preferred Stock, Series A	—	125,000
Common stock, $.01 par value; 150,000,000 shares authorized, 48,353,999 shares issued and outstanding	—	484
Additional capital	—	676,224
Retained earnings	—	866,123
TOTAL SHAREHOLDERS' EQUITY (DEFICIT)	(150,411)	1,667,831
	$5,382,153	$3,300,447

See notes to consolidated financial statements.

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(Dollars in thousands, except per-share data)

	Successor	Predecessor		
	Five months ended December 31, 1987	Seven months ended July 31, 1987	Year ended December 31 1986	1985
REVENUES:				
Net sales	$3,211,018	$4,865,436	$7,782,664	$7,856,663
Other income	14,616	33,938	40,312	43,514
	3,225,634	4,899,374	7,822,976	7,900,177
COST OF SALES AND EXPENSES:				
Cost of goods sold (including $458,179, $632,082, $983,609 and $1,566,691 from related parties)	2,463,896	3,853,040	6,072,019	6,254,158
Selling, general and administrative expenses	827,006	946,491	1,531,931	1,423,611
Interest expense (including $1,779, $1,658, $3,683 and $4,080 to related parties)	163,515	45,081	57,291	56,529
Contributions to Employees' Savings and Profit Sharing Plan	6,926	10,844	21,406	27,722
	3,461,343	4,855,456	7,682,647	7,762,020
	(235,709)	43,918	140,329	138,157
GAIN FROM SALE OF HALF-INTEREST IN CITGO	—	23,254	114,732	—
EARNINGS (LOSS) BEFORE INCOME TAXES, EQUITY IN EARNINGS OF CITGO AND BUSINESS UNITS TO BE DIVESTED	(235,709)	67,172	255,061	138,157
INCOME TAXES (BENEFIT)	(71,785)	31,410	24,491	54,321
EQUITY IN EARNINGS (LOSS) OF CITGO (pretax in 1986 and 1985)	14,177	39,131	(51,993)	112,675
EARNINGS (LOSS) BEFORE BUSINESS UNITS TO BE DIVESTED	(149,747)	74,893	178,577	196,511
EARNINGS OF BUSINESS UNITS TO BE DIVESTED (net of income taxes of $11,456, $21,009 and $15,395)	—	15,185	21,868	16,024
NET EARNINGS (LOSS)	(149,747)	90,078	200,445	212,535
ACCRETION TO REDEMPTION VALUE OF REDEEMABLE PREFERRED STOCK	(263)	—	—	—
PREFERRED STOCK DIVIDENDS:				
Series A	(88)	(5,822)	(10,000)	(3,428)
Redeemable	(580)	—	—	—
NET EARNINGS (LOSS) APPLICABLE TO COMMON SHARES	$ (150,678)	$ 84,256	$ 190,445	$ 209,107
EARNINGS (LOSS) PER COMMON SHARE:				
Before business units to be divested:				
Primary	$(.75)	$1.42	$3.51	$4.07
Fully diluted	$(.75)	$1.42	$3.49	$4.04
Net earnings (loss) applicable to common shares:				
Primary	$(.75)	$1.74	$3.96	$4.41
Fully diluted	$(.75)	$1.74	$3.91	$4.37

See notes to consolidated financial statements.

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(Dollars in thousands, except per-share data)

	Successor	Predecessor		
	Five months ended December 31, 1987	Seven months ended July 31, 1987	Year ended December 31 1986	1985
PREFERRED STOCK, SERIES A:				
Balance, beginning of period	$ 124,450	$ 125,000	$ 125,000	$ 125,000
Conversion to common stock	(102)	(550)	—	—
Retired in Tender and Merger	(124,348)	—	—	—
Balance, end of period	—	124,450	125,000	125,000
COMMON STOCK:				
Balance, beginning of period	489	484	476	471
Conversion of debt	—	—	1	2
Stock options, incentives and other	—	5	7	3
Purchased in Tender and Merger	(489)	—	—	—
Issued in Merger	2,000	—	—	—
Balance, end of period	2,000	489	484	476
ADDITIONAL CAPITAL:				
Balance, beginning of period	698,386	676,224	639,871	630,517
Conversion of debt	—	1,089	2,150	5,012
Stock options, incentives and other	942	21,073	34,203	4,342
Adjustment for Merger	(684,741)	—	—	—
Balance, end of period	14,587	698,386	676,224	639,871
RETAINED EARNINGS (DEFICIT):				
Balance, beginning of period	924,079	866,123	731,476	564,699
Net earnings (loss)	(149,747)	90,078	200,445	212,535
Cash dividends:				
Common stock ($.56 per share in 1987)	—	(27,145)	(53,877)	(47,405)
Preferred Stock, Series A ($3.00 per share in 1987)	(2,577)	(5,000)	(10,000)	(2,150)
Dividends on redeemable preferred stock	(580)	—	—	—
Stock options	(226)	(1,314)	(2,681)	(621)
Accretion to redemption value of redeemable preferred stock	(263)	—	—	—
Foreign currency translation adjustment	677	1,337	760	4,418
Adjustment for Merger	(938,361)	—	—	—
Balance, end of period	(166,998)	924,079	866,123	731,476
TOTAL SHAREHOLDERS' EQUITY (DEFICIT)	$(150,411)	$1,747,404	$1,667,831	$1,496,823

See notes to consolidated financial statements.

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

(Dollars in thousands)

	Successor	Predecessor		
	Five months ended December 31, 1987	Seven months ended July 31, 1987	Year ended December 31 1986	Year ended December 31 1985
INTERNALLY GENERATED FUNDS:				
Earnings (loss) before business units to be divested	$ (149,747)	$ 74,893	$ 178,577	$ 196,511
Noncash items:				
Depreciation and amortization of property, plant and equipment	91,582	113,793	161,945	143,841
Other amortization	13,756	—	—	—
Deferred income taxes	(10,505)	2,758	(1,887)	(2,771)
Equity in (earnings) loss of Citgo	(13,784)	(37,405)	58,896	(73,002)
Interest expense	29,137	—	—	—
	(39,561)	154,039	397,531	264,579
Increase in accounts payable and accrued expenses	109,634	55,393	52,461	67,583
(Decrease) increase in accounts payable to related parties	(7,694)	13,850	(45,548)	47,515
(Increase) decrease in deposits and prepaid expenses	(4,672)	(514)	5,354	(3,752)
Decrease (increase) in inventories	75,570	(415)	(57,302)	(59,845)
(Increase) decrease in accounts and notes receivable	(8,147)	181	(9,399)	(9,319)
(Decrease) increase in income taxes	(67,602)	13,074	(26,538)	62,357
Increase (decrease) in deferred credits and other liabilities	51,454	(22,516)	44,682	21,897
Funds provided from operations	108,982	213,092	361,241	391,015
Funds used to pay dividends on common stock	—	(27,145)	(53,877)	(47,405)
Funds used to pay dividends on preferred stock	(2,577)	(5,000)	(10,000)	(2,150)
Net change in accumulated foreign currency translation adjustment	677	1,337	760	4,418
NET INTERNALLY GENERATED FUNDS AVAILABLE FOR INVESTMENT	107,082	182,284	298,124	345,878
CAPITAL INVESTMENT ACTIVITIES:				
Acquisitions:				
Property, plant and equipment	(157,528)	(403,095)	(626,144)	(387,988)
Net noncurrent assets of businesses acquired	(10,831)	(2,604)	(63,464)	(8,302)
Investment in properties	15,400	9,000	35,600	7,400
	(152,959)	(396,699)	(654,008)	(388,890)
Other	(112,054)	(86,431)	(32,438)	16,647
Retirements of property, plant and equipment	23,602	22,500	43,210	47,659
Investment in and advances to Citgo	100,000	—	299,979	(272,562)
Sale of half-interest in Citgo	—	—	147,814	—
Equity purchased by JT Acquisition:				
Preferred stock, Series A	(120,295)	—	—	—
Common stock	(703,869)	—	—	—
Retained earnings	(938,361)	—	—	—
	(1,762,525)	—	—	—

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION (Continued)

(Dollars in thousands)

	Successor	Predecessor		
	Five months ended December 31, 1987	Seven months ended July 31, 1987	Year ended December 31 1986	1985
CAPITAL INVESTMENT ACTIVITIES (continued):				
Revaluation for Merger:				
Property, plant and equipment	$ (192,211)	$ —	$ —	$ —
Investment in and advances to Citgo	(142,264)	—	—	—
Excess of cost over fair value of net assets	(939,215)	—	—	—
Other assets	(355,612)	—	—	—
Net current assets	(141,740)	—	—	—
Other noncurrent liabilities	(73,528)	—	—	—
Other assets held for sale	(44,474)	—	—	—
	(1,889,044)	—	—	—
NET FUNDS USED IN CAPITAL INVESTMENT ACTIVITIES	(3,792,980)	(460,630)	(195,443)	(597,146)
FINANCING ACTIVITIES:				
Financing acquired:				
Commercial paper and notes payable to banks	—	9,434	—	174,380
Long-term debt	4,011,889	332,575	34,332	54,185
Sale of accounts receivable	—	—	(40,914)	1,289
Common stock	17,300	20,835	33,680	12,812
Preferred stock, Series A	(99)	(532)	—	120,926
Redeemable preferred stock	91,288	—	—	—
Dividends and accretion to redemption value of redeemable preferred stock	(843)	—	—	—
Common stock purchase warrants	26,136	—	—	—
	4,145,671	362,312	27,098	363,592
Discharge of commercial paper and notes payable to banks	(424,725)	—	(31,329)	—
Discharge of long-term debt (including $1,922, $2,555, $3,390 and $5,007 to related parties)	(143,350)	(16,407)	(34,119)	(51,428)
NET FUNDS PROVIDED BY (USED IN) FINANCING ACTIVITIES	3,577,596	345,905	(38,350)	312,164
BUSINESS UNITS TO BE DIVESTED:				
Net earnings and noncash expenses	—	32,033	45,445	35,834
Increase in net current assets	—	(12,696)	(23,879)	(6,708)
Additions of property, plant and equipment	—	(30,768)	(92,534)	(68,564)
Increase in other net noncurrent assets	—	(1,343)	610	8,243
Retirements of property, plant and equipment	—	6,077	2,850	1,695
Revaluation of business units to be divested	(7,667)	—	—	—
NET FUNDS USED BY BUSINESS UNITS TO BE DIVESTED	(7,667)	(6,697)	(67,508)	(29,500)
(DECREASE) INCREASE IN CASH AND SHORT-TERM INVESTMENTS	$ (115,969)	$ 60,862	$ (3,177)	$ 31,396

See notes to consolidated financial statements.

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 1987

1. ***MERGER WITH JT ACQUISITION CORPORATION:***

On July 3, 1987, The Southland Corporation (referred to collectively with its subsidiaries as the Company) entered into a definitive Agreement and Plan of Merger (the Agreement) with JT Acquisition Corporation (JT), a corporation organized at the direction of The Thompson Company, pursuant to which the Company agreed to be acquired by JT in a two-step transaction. John P. Thompson and Jere W. Thompson, officers and directors of the Company, and Joe C. Thompson, Jr., a director of the Company, are indirect owners of The Thompson Company.

In the first-step tender offer (the Tender), on August 1, 1987, JT accepted for payment 31,500,000 shares of the Company's common stock at $77 per share in cash and 2,418,949 shares of the Company's Preferred Stock, Series A at $90.27 per share in cash. JT already owned 2,597,403 shares of the Company's common stock, giving it control of approximately 70% of the outstanding common shares and 97% of the outstanding preferred shares. Pursuant to the Agreement, in the second-step merger, which was consummated on December 15, 1987 (the Merger), JT was merged into the Company with the Company continuing as the surviving corporation. As a result of the Merger, each remaining common share of the Company was converted into $61.32 in cash and 0.6672 of a share of a new class of cumulative exchangeable preferred stock of the Company with a stated value of $25 per share (or approximately $16.68 of stated value for each common share converted in the Merger). Each remaining share of Preferred Stock, Series A was cancelled and exchanged for $90.27 in cash. The Merger has been accounted for as if it occurred on December 31, 1987.

On August 1, 1987, immediately prior to the expiration of the Tender, the preferred stock purchase rights previously issued to holders of common shares were redeemed for $.05 per right.

Details of the financing of the Tender and the Merger are provided in Notes 12, 13 and 15.

The Merger was accounted for under the purchase method as a step acquisition. As a result, the consolidated financial statements for the year ended December 31, 1987, are comprised of different periods within the year reported on different accounting bases, as follows:

Period	Accounting basis
Predecessor Company:	
January 1, 1987 — July 31, 1987	Historical basis
Successor Company:	
August 1, 1987 — December 31, 1987	Historical basis — one-third of net assets New purchase accounting basis — two-thirds of net assets
As of December 31, 1987	New purchase accounting basis

For purposes of establishing the new purchase accounting basis, the debt of JT used to finance the Tender and the Merger, along with related interest expense and other costs, was pushed down into the Company's accounts.

The Company has not changed the tax basis of its net assets in connection with the Merger. The purchase accounting adjustments for property, plant and equipment; investment in Citgo; and certain other assets and liabilities (including reserves not deductible for income tax purposes) were recorded net of the income tax effect of the differences between the fair values and the carryover income tax bases of these accounts. Depreciation and amortization of the purchase accounting adjustments will not be recognized for income tax purposes.

1. *MERGER WITH JT ACQUISITION CORPORATION (Continued):*

Subsequent to August 1, 1987, the assets held for sale and business units to be divested have been recorded at their estimated net realizable values, net of the income tax effect of the differences between those values and the carryover tax bases. The estimated net realizable values include an estimated selling price, an estimate of net cash flow for these operations from August 1, 1987, through the estimated date of disposition, and interest expense of $21,600,000 allocated to the operations as if the purchase of the net assets of these operations was financed entirely by debt from the Merger. A net loss of $9,300,000 from operations of these properties to be sold, including allocated interest and income taxes, was excluded from consolidated operating results for the five months ended December 31, 1987, in accordance with generally accepted accounting principles.

As a result of the above, the results of operations of the Company subsequent to the Tender and the Merger are not comparable to those of any period prior to the Tender or the Merger.

The allocation of JT's purchase price of the Company, as included in these financial statements, is necessarily tentative and is expected to be refined in the future. Any differences are not expected to be material.

The following table summarizes unaudited pro forma financial information as if the acquisition of the Company by JT occurred on January 1 of each year presented. The pro forma financial information does not purport to be indicative of the results which would actually have been obtained had such transactions been completed as of the assumed date for the periods presented, or which may be obtained in the future.

	Year ended December 31	
	1987	1986
	(Dollars in thousands)	
Revenues	$7,251,472	$6,965,838
Net loss	(491,687)	(592,213)
Primary loss per share	(2.68)	(3.18)

2. *ACCOUNTING POLICIES:*

Principles of Consolidation

The Southland Corporation is wholly owned by affiliates of The Thompson Company, a Texas corporation. The consolidated financial statements include the accounts of The Southland Corporation and its subsidiaries and, subsequent to August 1, 1987, the accounts of JT. Intercompany transactions are eliminated.

The Company's investment in Citgo Petroleum Corporation (Citgo) is accounted for by the equity method. Accordingly, this investment is shown on the consolidated balance sheets at historical cost to the Company prior to August 1, 1987, and at cost determined by purchase accounting subsequent to August 1, 1987, plus equity in undistributed earnings (see Note 3). Equity in earnings (loss) of Citgo on the consolidated statements of operations represents, after elimination of intercompany interest, the Company's 100% interest in Citgo on a pretax basis through September 30, 1986, and its 50% interest on an after-tax basis after that date. At December 31, 1987, the Company's investment in Citgo exceeded its equity in net assets by $151,460,000 as a result of purchase accounting pursuant to the Tender and the Merger. Equity in earnings of Citgo is reduced for the amortization of these intangibles (straight-line over 40 years), which arose pursuant to the Merger.

2. *ACCOUNTING POLICIES (Continued):*

Principles of Consolidation (Continued)

Financial information provided by Citgo, not including eliminations recorded in the Company's consolidated financial statements, is summarized as follows:

	December 31	
	1987	1986
	(Dollars in thousands)	
Summary of financial position:		
Current assets	$ 766,325	$ 826,123
Noncurrent assets	424,247	382,474
	$1,190,572	$1,208,597
Current liabilities	$ 390,340	$ 307,191
Noncurrent liabilities	375,381	562,280
Shareholders' equity	424,851	339,126
	$1,190,572	$1,208,597

	Year ended December 31		
	1987	1986	1985
	(Dollars in thousands)		
Summary of operating results:			
Revenues	$3,967,964	$4,132,129	$5,716,024
Gross profit	200,423	114,008	181,850
Net earnings	85,725	43,578	39,291

Prior to September 30, 1986, Citgo was included in the Company's consolidated income tax return. For financial reporting prior to January 1, 1986, the Company allocated tax expense (benefit) to Citgo based on pretax earnings (loss) using the Company's consolidated effective tax rate. In connection with its negotiations to sell 50% of the common stock of Citgo, the Company agreed to pay Citgo certain of the tax benefits related to Citgo and utilized in the Company's consolidated tax return for the period from January 1, 1986 through September 30, 1986. The amount of these tax benefits was approximately $50,000,000 and has been included as a tax benefit in Citgo's operating results for 1986. The allocation of intercompany taxes had no effect on the Company's reported earnings. If taxes for Citgo for the years ended December 31, 1986 and 1985, had been calculated on a stand-alone basis as if Citgo had not been a subsidiary of the Company, pro forma net earnings for Citgo for those years would have been $7,354,000 and $59,700,000.

2. *ACCOUNTING POLICIES (Continued):*

Principles of Consolidation (Continued)

Citgo has investments in various pipeline companies consisting of 6.8% to 50% interests. Financial information relating to these pipeline companies, provided by Citgo, is summarized as follows:

	December 31	
	1987	1986
	(Dollars in thousands)	
Summary of financial position:		
Current assets	$ 102,629	$ 101,225
Noncurrent assets	1,117,033	1,151,140
	$1,219,662	$1,252,365
Current liabilities	$ 185,278	$ 183,925
Noncurrent liabilities	943,994	979,977
Shareholders' equity	90,390	88,463
	$1,219,662	$1,252,365

	Year ended December 31		
	1987	1986	1985
	(Dollars in thousands)		
Summary of operating results:			
Revenues	$725,025	$742,543	$690,159
Gross profit	421,537	425,489	406,597
Net earnings	212,936	193,682	175,009

Revenues

Net sales are comprised of sales of products and services, including sales by stores operated by franchisees of $1,161,485,000, $1,570,963,000, $2,529,157,000 and $2,287,554,000 from 3,064, 3,030, 2,938 and 2,849 stores for the five months ended December 31, 1987, the seven months ended July 31, 1987, and the years ended December 31, 1986 and 1985. There is no significant difference in the profitability of a Company-operated and a franchisee-operated store.

Sales by stores operated under domestic and foreign area license agreements are not included. All fees or royalties arising from such agreements are included in other income. Initial fees, which have been immaterial, are recognized when the services required under the agreements are performed.

Other income is primarily comprised of area license royalties, gains from the sale of assets no longer used in the business and interest on short-term investments.

Business Units to Be Divested

The business units to be divested (see Note 8) were accounted for as discontinued operations of a segment of the business through July 31, 1987, in accordance with Accounting Principles Board Opinion No. 30. As a result, the related financial information is segregated on the Company's consolidated financial statements, and the financial statements for years prior to 1987 have been restated to conform to that presentation. Subsequent to July 31, 1987, they are valued in accordance with purchase accounting (see Note 1).

2. *ACCOUNTING POLICIES (Continued):*

Cost of Goods Sold

Cost of goods sold includes buying and occupancy expenses.

Inventories

Inventories are stated at the lower of cost or market, which, as to merchandise in stores, is determined by the retail inventory method. Cost is determined using the LIFO method for substantially all inventories.

Investment in Properties

Investment in properties, which relates to years prior to 1987, includes land, buildings and equipment to be sold for cash and leased back under operating lease agreements, as well as closed stores held for sale. The Company expected that cash would be realized for these properties within a 12-month period. Working capital was used in the acquisition, construction and carrying of these assets.

Depreciation and Amortization

Depreciation of buildings and equipment is based upon the estimated useful lives of these assets using the straight-line method. Amortization of capital leases, improvements to leased properties and favorable leaseholds is based upon the remaining terms of the leases or the estimated useful lives, whichever is shorter.

Excess of Cost Over Fair Value of Net Assets Acquired

The excess of the purchase price over the fair value of Southland's net assets acquired in the Merger is recorded at cost less accumulated amortization (straight-line basis over 40 years) of $7,400,000.

Excise Taxes

Excise taxes of $186,186,000, $261,753,000, $390,833,000 and $336,872,000 collected from customers on retail gasoline sales are included in net sales and cost of goods sold for the five months ended December 31, 1987, the seven months ended July 31, 1987, and the years ended December 31, 1986 and 1985.

Income Taxes and Investment Tax Credits

Income taxes are the estimated amount of federal and state income taxes on earnings reported in the consolidated statements of earnings. Deferred taxes and deferred tax benefits are provided for and are a result of timing differences between financial and tax reporting.

Investment tax credits were recorded as a reduction of income taxes in the year the related assets were placed in service (see Note 19).

Leases

Capital leases are recorded at the inception of the lease at the lower of the discounted present value of future minimum lease payments or the fair value of the property.

For closed leased stores, provision is made on a current basis if anticipated expenses are in excess of expected sublease rentals.

2. *ACCOUNTING POLICIES (Continued):*

Business Segment

The Company (Successor) operates in a single business segment — the operating and franchising of convenience food stores, primarily under the 7-Eleven name.

3. *SALE OF HALF-INTEREST IN CITGO AND ACCOUNTING CHANGE:*

As of September 30, 1986, the Company sold 50% of the common stock of Citgo to an indirect wholly owned subsidiary of Petroleos de Venezuela, S.A. (PDVSA), the Venezuelan national oil company. The purchase price consisted of $290,000,000 cash. In connection with the purchase, Citgo entered into a 20-year crude supply agreement with PDVSA to purchase a minimum of 130,000 barrels of crude oil per day at market-related prices, and the Company entered into a 20-year product purchase agreement with Citgo to buy specified quantities of gasoline at market-related prices (see Note 21).

The sale resulted in a gain to the Company during 1986 of $114,700,000 before profit sharing expense of $11,400,000 and income taxes of $14,700,000, for a net gain of $88,600,000. During the first quarter of 1987, the remaining $23,300,000 gain, before profit sharing expense of $2,400,000 and income taxes of $5,600,000 for a net gain of $15,300,000, was recognized.

The financial statements for all periods prior to September 30, 1986, reflect the Company's 100% ownership of Citgo on the equity method before deductions for income taxes and profit sharing expense, which are separately provided in the consolidated statements of operations. Financial statements for periods subsequent to September 30, 1986, reflect the Company's 50% ownership of Citgo on the equity method after deductions for income taxes provided in the accounts of Citgo.

4. *CASH AND SHORT-TERM INVESTMENTS:*

Cash and short-term investments include temporary cash investments of $49,352,000 and $105,718,000 at December 31, 1987 and 1986, stated at cost, which approximates market.

5. *ACCOUNTS AND NOTES RECEIVABLE:*

	December 31	
	1987 (Successor)	1986 (Predecessor)
	(Dollars in thousands)	
Notes receivable (net of long-term portion of $10,258 and $15,077)	$ 3,654	$ 9,838
Trade accounts receivable	71,324	75,100
Franchisee accounts receivable	50,430	31,566
Refundable income taxes	33,196	—
	158,604	116,504
Allowance for doubtful accounts	(6,594)	(4,028)
	$152,010	$112,476

6. *INVENTORIES:*

At December 31, 1987 and 1986, inventories stated on the LIFO basis were approximately \$261,916,000 and \$283,408,000, which is less than replacement cost by approximately \$10,673,000 and \$83,124,000. At December 31, 1987, after the application of purchase accounting pursuant to the Tender and Merger, inventories for financial statement purposes exceeded the tax LIFO basis of those inventories by \$54,656,000.

7. *PROPERTY, PLANT AND EQUIPMENT:*

	December 31	
	1987 (Successor)	1986 (Predecessor)
	(Dollars in thousands)	
Cost:		
Land	\$ 704,506	\$ 456,252
Buildings and leaseholds	1,130,254	1,143,171
Machinery and equipment	548,273	909,239
Construction in process	102,444	355,447
	2,485,477	2,864,109
Accumulated depreciation and amortization	(141,028)	(844,238)
	\$2,344,449	\$2,019,871

In 1984, the Company commenced construction of a new corporate headquarters tower in Dallas, Texas. Remaining construction costs to complete the tower are expected to approximate \$100,000,000.

8. *BUSINESS UNITS TO BE DIVESTED:*

As of August 1, 1987 (the date the Tender was closed), the Company decided to sell several business units, consisting of its Dairies Group, Chief Auto Parts, Reddy Ice, Tidel Systems, Southland Chemical/Food Labs and Snack Foods Division. These operations are classified as business units to be divested, and the related financial information is segregated on the Company's consolidated financial statements in accordance with the provisions of Accounting Principles Board Opinion No. 30 relating to discontinued operations of a segment of a business. The consolidated financial statements and notes thereto for periods prior to August 1, 1987, have been restated to retroactively reflect that treatment of the business units to be divested.

Earnings of business units to be divested include expenses which are charged to operations based upon the actual cost of the services provided and certain other expenses which are allocated based upon usage of the services. In addition, prior to the Merger, only interest expense related to debt which is anticipated to be assumed was charged against operations of the business units. Profit sharing expense is calculated at 10% of pretax earnings for years prior to 1987, and on a pro rata basis based on number of employees in 1987, and income tax expense is calculated at statutory rates. Management believes that these allocations represent reasonable allocations of expenses to the business units. No other corporation expenses have been allocated to the business units to be divested since management believes that such expenses will not be materially decreased due to such divestitures, and, accordingly, these expenses remain in continuing operations.

8. *BUSINESS UNITS TO BE DIVESTED (Continued):*

See Note 1 for a discussion of the valuation of business units to be divested subsequent to August 1, 1987.

Revenues for these operations for the five months ended December 31, 1987, the seven months ended July 31, 1987, and the years ended December 31, 1986 and 1985, were $353,000,000, $533,000,000, $797,000,000 and $722,000,000.

It is anticipated that these operations will be sold for cash and that the majority of the sales will be completed in 1988. Because these assets are carried at expected net realizable value, no gain or loss on their disposal will be recognized.

9. *OTHER ASSETS HELD FOR SALE:*

In connection with financing the Tender and the Merger, the Company also announced its intention to sell certain assets other than the business units to be divested (see Note 8), including approximately 1,000 operating store properties, the MovieQuik videotape rental division, 250 vacant store sites, surplus land and miscellaneous other properties. Because these properties do not comprise a segment of the Company's business, prior financial statements have not been restated to reflect these divestitures. See Note 1 for a discussion of the valuation of other assets held for sale subsequent to the Merger.

Revenues for these properties for the five months ended December 31, 1987, the seven months ended July 31, 1987, and the years ended December 31, 1986 and 1985, were $367,000,000, $513,000,000, $857,000,000 and $960,000,000.

It is anticipated that these properties will be sold for cash and that the majority of the sales will be completed in 1988. Because these properties are carried at expected net realizable value, no gain or loss on their disposal will be recognized.

10. *OTHER ASSETS:*

As a result of the application of purchase accounting pursuant to the Merger, the Company has recorded $376,000,000 (less accumulated amortization of $6,000,000 at December 31, 1987) in other assets representing the fair value of future royalty payments from foreign and domestic area license agreements. The value of the future royalties will be amortized over 20 years using the straight-line method, and income will be recognized for the actual payment of royalty fees. During the first quarter of 1988, the Company monetized its future royalty payments from the area licensee in Japan through a limited recourse loan, payable in Japanese yen, for approximately $325,000,000. Future royalties from the area licensee in Japan, as well as certain trademarks, were pledged for the term of the loan as security against the loaned amount.

11. *ACCOUNTS PAYABLE AND ACCRUED EXPENSES:*

	December 31 1987	December 31 1986
	(Dollars in thousands)	
Trade accounts payable	$323,096	$264,033
Accrued payroll	55,823	76,447
Accrued taxes	56,244	71,590
Payable to employees for redemption of stock options and related taxes and benefits	65,649	6,737
Interest payable	24,647	8,052
Other	120,403	112,981
	$645,862	$539,840

12. *DEBT:*

	December 31, 1987 Amount outstanding	Due within one year	Balance included in long-term debt
	(Dollars in thousands)		
Term loans under Credit Agreement	$2,494,608	$564,000	$1,930,608
15¾% Senior Subordinated Notes due 1997	350,000	—	350,000
16½% Senior Subordinated Discount Notes due 1997	251,833	—	251,833
16¾% Subordinated Debentures due 2002	500,000	—	500,000
18% Junior Subordinated Discount Debentures due 2007	376,893	—	376,893
12% Canadian notes due 1992	38,601	—	38,601
Real estate and equipment notes and other debt with a weighted average effective interest rate of 9.6% (mature 1988 to 2011)	73,972	6,463	67,509
9.3% Canadian Term Loan	19,237	19,237	—
Revolving credit facility	25,000	25,000	—
7⅞% Cityplace notes	275,458	—	275,458
Capital lease obligations	200,644	12,644	188,000
	$4,606,246	$627,344	$3,978,902

Bank Credit Agreement

On December 15, 1987, the date of the Merger, the Company became obligated under a Credit Agreement which includes a Senior Term Loan of $2,000,000,000 and a Divestiture Term Loan of $494,608,000. In addition, a revolving credit facility of $450,000,000 is included under the terms of the Credit Agreement.

Fees paid and deferred relative to the Tender and Merger loans totaled approximately $73,000,000, of which the majority was facility fees, and will be amortized over the life of the Credit Agreement using the interest method.

12. *DEBT (Continued):*

Bank Credit Agreement (Continued)

The Credit Agreement contains numerous financial and operating covenants requiring, among other things, the maintenance of certain financial ratios, including interest coverage, fixed-charge coverage and total debt. In addition, the Credit Agreement requires the attainment of certain levels of earnings before interest, income taxes and depreciation and amortization. In the event the Company fails to comply with these covenants and other restrictions discussed below, it could be in default under the agreement, and substantially all of the Company's long-term debt maturities could be accelerated.

In addition, the Credit Agreement contains various covenants which, among other things, (a) limit the Company's ability to incur indebtedness or other liabilities other than under the Credit Agreement, (b) restrict the Company's ability to engage in sales and leasebacks, (c) limit future capital expenditures and (d) restrict the Company's ability to pay cash dividends, exchange Merger Preferred shares for subordinated debt, redeem or prepay principal and interest on any subordinated debt and repurchase common stock purchase warrants. The Credit Agreement further provides that the banks receive, with the exception of certain specified property, a security interest in all of the assets of the Company.

Interest is payable quarterly on the Senior Term Loan, the Divestiture Term Loan and the revolving credit facility at a variable rate equal to the lead bank's base rate plus 1.5% per year or, at the Company's option, at a rate equal to a reserve-adjusted Eurodollar rate plus 2.5% per year. The applicable rate at December 31, 1987, was 10-¼%.

The Senior Term Loan must be fully paid on December 31, 1995, and is to be paid through minimum installments of $300,000,000 on both December 31, 1988, and December 31, 1989, and quarterly installments ranging from $37,500,000 to $75,000,000 commencing March 31, 1990 through December 31, 1995. The Divestiture Term Loan is payable in minimum installments of $45,000,000 on December 31, 1988, $175,000,000 on June 30, 1989, and $275,000,000 on December 31, 1989.

The Company has agreed to sell certain business units and other assets (see Notes 8 and 9). The net proceeds of these sales are required to be used to prepay the minimum installments on the Divestiture Term Loan and the Senior Term Loan. Because the sales proceeds from the divestitures that are expected during 1988 exceed the minimum installments required for both term loans, the greater amount has been classified as due within one year at December 31, 1987. In addition, the Senior Term Loan will be further reduced by $300,000,000 in proceeds from the monetization of future royalty payments (see Note 10).

The $450,000,000 available under the revolving credit facility will be reduced to $400,000,000 on December 31, 1990, and to $350,000,000 on December 31, 1991. The revolving credit facility will expire, and all amounts outstanding will be due and payable in full, on December 31, 1992. The facility includes requirements for an annual repayment for 30 consecutive days of all revolving loans outstanding. The amount outstanding under the facility as of December 31, 1987, was $25,000,000 at a rate of 10-¼% and is classified as a current liability because it was repaid during the first quarter of 1988. The facility provides for up to $200,000,000 for letters of credit, and to the extent that they are issued, the amount available for borrowing under the revolving credit facility is reduced. At December 31, 1987, $135,000,000 in letters of credit was outstanding. A fee of 2% per year on the outstanding amount of letters of credit is required to be paid monthly. A ½% per year commitment fee on unadvanced funds, which for purposes of this calculation include outstanding letters of credit, is payable quarterly.

12. *DEBT (Continued):*

Bank Credit Agreement (Continued)

Under the Credit Agreement, the Company is required to have interest rate contracts by which it is protected against increases in short-term interest rates for 50% of the then-outstanding amount of the term loans after one year.

Debentures and Notes

On December 15, 1987, the Company issued four series of debentures and notes for net cash proceeds of $1,500,000,000 in connection with the financing of the Merger.

The $350,000,000 15-3/4% Senior Subordinated Notes provide for a sinking fund payment equal to one-half of the principal amount outstanding on December 15, 1996, and are to be paid in full by December 15, 1997. Interest payments are to be made semiannually, commencing on June 15, 1988. These notes are redeemable at the option of the Company from December 1992 through December 1993 at 105% of principal, from December 1993 through December 1994 at 102.5% of principal and thereafter until maturity at 100% of principal.

The $402,260,000 16-1/2% Senior Subordinated Discount Notes were issued at a discount of $152,260,000 from their principal amount. The discount will be accreted through December 15, 1990, resulting in an effective interest rate of 16-1/2% through that date. These notes require semiannual interest payments at an annual rate of 16-1/2% beginning June 15, 1991. The discount notes require no sinking fund payments and are redeemable at the Company's option at any time, in whole or in part, at 100% of principal. The notes are due December 15, 1997.

The $500,000,000 16-3/4% Subordinated Debentures require sinking fund payments equal to 20% of the principal amount on December 15 each year, commencing in 1998. These debentures are redeemable at the Company's option at amounts ranging from 106% of principal beginning December 1992 to 101-1/2% in December 1995. Beginning December 1996, they may be redeemed at 100% of principal until maturity. The notes are to be paid in full by December 15, 2002. Semiannual interest payments begin June 15, 1988.

The $946,945,000 Junior Subordinated Discount Debentures were issued in 946,945 units, each consisting of a $1,000 debenture and 27.6 common stock purchase warrants (see Note 15). These debentures were issued at a discount of $573,081,000 from their principal amount. The discount will be accreted through December 15, 1992, resulting in an effective interest rate of 18.3%, and require semiannual interest payments at an annual rate of 18.0% beginning June 15, 1993. Sinking fund payments are required on December 15, 2003 through 2007, each for 20% of the principal amount. The debentures are redeemable at the Company's option at any time at 100% of principal.

Fees paid and deferred relative to the debentures and notes totaled approximately $72,000,000, the majority of which was underwriting costs, and will be amortized over the life of the debt using the interest method.

All of the debentures and notes are subordinate to the bank loans outstanding under the Credit Agreement; to previously outstanding mortgages and notes that are backed by specific collateral or are general unsecured, unsubordinated obligations; and in several cases, to each other.

12. *DEBT (Continued):*

Other Debt

During 1984, the Company entered into currency exchange agreements that converted $75,000,000 of floating rate debt into Japanese yen equivalents bearing interest at 7.7% on a quarterly payment basis, payable in Japanese yen for seven to ten years. These agreements were hedged by the Company's future yen royalty receipts from its area licensee in Japan, and accordingly, no foreign currency exchange rate gain or loss was recognized on these yen borrowings until late 1987, when the Company decided to monetize and unhedge the future yen royalties (see Note 10), and a loss of $55,500,000 was recognized as a result of exchange rate differences relating to future payments due under the exchange agreements. The Company also has an interest rate exchange agreement which fixes the interest rate on $100,000,000 of floating rate debt until December 1989. The Company receives a sum based on the six-month LIBOR and pays at a rate of 11.7%. In 1988 and late 1987, the Company entered into similar agreements fixing $515,000,000 of debt for from two to four years paying at rates averaging 9.1%. Additionally, the Company entered into one- to four-year agreements which provide for payments to be made to it to cover incremental interest costs on $315,000,000 if the three-month LIBOR exceeds 9% and on $50,000,000 if the rate exceeds 9.5%.

Cityplace Center East Corporation, a subsidiary of the Company, issued $290,000,000 of notes in March 1987 to finance the construction of the headquarters tower, a parking garage and related facilities of the Cityplace Center development. These notes bear interest at 7-7/8%, payable semi-annually, with the principal amount due February 15, 1995. After the application of purchase accounting pursuant to the Merger, the effective interest rate on the notes for financial statement purposes is 8.5%. Principal and interest on the notes are payable by drawings under irrevocable letters of credit issued by The Sanwa Bank, Limited, Dallas Agency, which, along with the note holders, has been granted a lien on the property financed. The Company will occupy a portion of the building as its corporate headquarters and attempt to sublease the rest. Payments under the Company's 15-year lease of the building and garage parking will be sufficient to cover interest on the debt and operating expenses.

The 12% Canadian notes due 1992 are redeemable at the option of the Company from July 1990 to July 1991 at 101-1/2% of the principal amount and after July 25, 1991, until maturity at 100-3/4% of principal. Payments of interest and principal are denominated in Canadian dollars.

In December 1987, the Company defeased the 8-3/8% debentures due 2002, the 9-3/8% debentures due 2003 and the 9-1/2% debentures due 2004 by depositing funds sufficient to pay the principal of the debentures and accrued interest through the January 14, 1988, date of redemption into a trusteed escrow account. The principal amount of these debentures was $113,712,000 and no longer appeared as a liability on the Company's records as of December 31, 1987. Prepayment penalties incurred as a result of this early extinguishment totaled $4,871,517, which has been recognized as an expense in the fourth quarter of 1987.

In April 1987, the Company's Canadian subsidiary entered into a term loan agreement under which it received Canadian $25,000,000 (approximately U.S. $19,000,000) at 9.3%. In December the agreement was terminated, and the balance due plus accrued interest was refinanced in January 1988 with a short-term revolving credit agreement of $25,000,000 with interest.

12. ***DEBT (Continued):***

Other Debt (Continued)

As of December 31, 1987, long-term debt scheduled maturities, which include capital lease obligations and sinking fund requirements, are as follows (dollars in thousands):

1988	$ 627,344
1989	552,146
1990	270,211
1991	169,883
1992	257,408
Thereafter	2,729,254
	$4,606,246

13. ***REDEEMABLE PREFERRED STOCK:***

The Company issued 9,911,647 shares of Junior Preferred Stock, 15% Cumulative Exchangeable Preferred Stock, Series One (the Redeemable Preferred) with an aggregate stated value of approximately $247,000,000, in connection with the Merger (see Note 1). The terms of the Redeemable Preferred provide that it will be fully redeemed by December 31, 2007. The Redeemable Preferred has a stated value and liquidation preference of $25.00 per share and will pay cumulative quarterly dividends at the annual amount of $3.75 per share, payable when and if declared by the Company's Board of Directors out of legally available funds. During the first 20 quarterly dividend periods after the effective date of the Merger, quarterly dividends on the Redeemable Preferred may be paid, at the Company's option, either in cash or in additional shares of Redeemable Preferred at the rate of $.9375 in cash or 0.0375 of a share of Redeemable Preferred. It is expected that, as a result of restrictions contained in the Credit Agreement, the first 20 quarterly dividend payments on the Redeemable Preferred will be paid in additional shares. Subject to restrictions contained in the Credit Agreement, the Redeemable Preferred may be redeemed, at the option of the Company, in whole or in part at any time prior to December 15, 1989, at $25.75 per share in cash and at any time thereafter at $25.00 per share in cash together with accrued but unpaid dividends. The Company must redeem at least 10% of the Redeemable Preferred each year 1998 through 2007 at a redemption price of $25.00 per share plus accrued but unpaid dividends. The Redeemable Preferred ranks junior in right of payment to long-term debt of the Company. The Redeemable Preferred is exchangeable after December 15, 1989, at the option of the Company and with the permission of the banks providing financing under the Credit Agreement, into debentures which will have an interest rate of 15% (which may be paid in additional debt securities until December 15, 1992). Such debentures would be subordinated to all other long-term debt and would mature in 2007. The debentures will be subject to mandatory redemption from 1998 through 2007 through sinking fund payments of 10% of the outstanding principal as of December 15, 1992.

The discount from stated value of approximately $157,300,000 is being accreted using the interest method. The Redeemable Preferred is recorded at redemption value less unaccreted discount.

The Company is authorized to issue 30,000,000 shares of junior preferred stock with rights and preferences, as determined by the Company's Board of Directors, 22,500,000 of which are authorized to be issued as redeemable preferred stock.

14. *PREFERRED STOCK:*

The Company has 5,000,000 shares of another class of preferred stock authorized for issuance. Any preferred stock issued will have such rights, powers and preferences as determined by the Company's Board of Directors. In connection with the Merger, the Company cancelled all outstanding shares of Cumulative Convertible Exchangeable Preferred Stock, Series A. At December 31, 1986, 2,500,000 shares of Series A were outstanding with a $50 per share stated and liquidation value.

15. *WARRANTS*:

In connection with the issuance of the 18% Junior Subordinated Discount Debentures, the Company issued 26,135,682 common stock purchase warrants (the Warrants). Each warrant entitles the holder to purchase one share of the Company's common stock at an exercise price of $1.00 in certain circumstances or to certain repurchase or other rights in lieu thereof. The Company has reserved 26,135,682 shares of common stock for the exercise of the Warrants.

The Warrants do not entitle the holders to receive dividends, vote, receive notice of any meetings of shareholders or otherwise have any rights as shareholders of the Company.

The Warrants may be exercised prior to December 16, 1992, if the Company (a) has a public offering of common stock or (b) is involved in certain business combinations. Otherwise, the Company is obligated to repurchase all outstanding Warrants by March 15, 1995, for cash or certain subordinated debt securities. The repurchase price will be the fair market value of the Warrants as separate securities, as determined by an independent financial expert chosen by the Company. Warrants not surrendered for exercise or repurchase as and when provided will expire and cease to exist in accordance with their terms.

The Company shall not be obligated to effect any repurchase that would constitute a violation or breach of applicable law or of the provisions of the Credit Agreement (see Note 12) or other loan agreements to which the Company is a party, in which case the Warrants will be exercisable. The Credit Agreement does not currently permit the Company to repurchase the Warrants for cash or debt securities of the Company.

The Warrants are recorded at current market value less the exercise price of $1.00 per share.

16. *EMPLOYEE BENEFIT PLANS:*

Employees' Savings and Profit Sharing Plan

Effective January 1, 1949, the Company adopted The Southland Corporation Employees' Savings and Profit Sharing Plan (Profit Sharing) for the purpose of providing retirement benefits for eligible employees.

Contributions to Profit Sharing are made by both the participants and the Company. The Company contributes the greater of approximately 10% of its net earnings before contribution to Profit Sharing and federal income taxes or any amount authorized by the Company's Board of Directors. The Company contribution is generally allocated to the participants on the basis of their individual contribution, years of participation in Profit Sharing and age. The Company contributions for the five months ended December 31, 1987, the seven months ended July 31, 1987, and the years ended December 31, 1986 and 1985, were $7,812,000, $13,804,000, $26,170,000 and $31,213,000.

16. *EMPLOYEE BENEFIT PLANS (Continued):*

Postretirement Insurance Benefits

Under a plan that covers both active and retired employees, the Company provides certain health care and life insurance benefits for retirees through a trust that is funded partially by their payments and the balance by the Company. Substantially all employees may become eligible for these retirement benefits if they reach normal retirement age or qualify for the Company's early retirement plan. The cost to the Company of retiree health care and life insurance benefits is recognized as expense as claims are incurred and was $574,000, $1,298,000, $1,909,000 and $1,442,000 for the five months ended December 31, 1987, the seven months ended July 31, 1987, and the years ended December 31, 1986 and 1985.

Stock Options

As a result of the Merger with JT, The Southland Corporation Employees' Stock Option Plan was terminated on December 15, 1987. Holders of outstanding options for 1,065,046 shares at December 15, 1987, were paid a total of $58,800,000, which, for some options, includes an additional amount equal to the difference between $78 per share ($61.32 cash paid for each share at the Tender plus $16.68 of stated value of Redeemable Preferred) and the exercise price of the option in accordance with the terms of the plan. Final payment was made on January 4, 1988. All outstanding options were cancelled at December 15, 1987. No options were granted in 1987. During the five months ended December 31, 1987, and the seven months ended July 31, 1987, options for 23,858 and 490,560 shares were exercised at $18.25 to $48.75 and $12.73 to $48.75 per share.

Key Employees Incentive Plan

As a result of the Merger with JT, the Key Employees Incentive Plan was terminated effective December 15, 1987. No shares were issued in 1987. In 1986 and 1985, 42,095 and 49,562 shares were issued under the plan.

Employee Stock Ownership Plan

Effective January 1, 1983, the Company adopted the Southland Employee Stock Ownership Plan (the ESOP) for eligible employees. Contributions to the ESOP totaled $3,380,000 and $3,031,000 for 1986 and 1985. The Company contribution was allocated to the participants on an equal basis and resulted in a federal tax credit of equal amount. The ESOP was terminated effective January 1987, and the assets were distributed to participants in 1987.

17. *LEASES AND CONTINGENCIES:*

Certain of the property, plant and equipment used in the Company's business is leased. Generally, real estate leases are for primary terms of from 14 to 20 years with options to renew for additional periods, and equipment leases are for terms of from five to ten years. The leases do not contain restrictions that have a material effect on the Company's operations.

17. *LEASES AND CONTINGENCIES (Continued):*

The composition of capital leases reflected as property, plant and equipment in the consolidated balance sheets is as follows:

	December 31	
	1987 (Successor)	1986 (Predecessor)
	(Dollars in thousands)	
Buildings	$ 156,533	$ 273,914
Equipment	12,307	36,328
	168,840	310,242
Accumulated amortization	(19,820)	(172,444)
	$ 149,020	$ 137,798

The present value of future minimum lease payments for capital lease obligations is reflected in the consolidated balance sheets as long-term debt. The amount representing imputed interest necessary to reduce net minimum lease payments to present value has been calculated generally at the Company's incremental borrowing rate at the inception of each lease.

Future minimum lease payments for years ending December 31 are as follows:

	Capital leases	Operating leases
	(Dollars in thousands)	
1988	$ 33,222	$ 123,944
1989	32,408	105,668
1990	31,412	100,319
1991	31,038	95,609
1992	30,231	91,125
1993 and thereafter	235,234	659,845
Future minimum lease payments	393,545	$1,176,510
Estimated executory costs	(2,356)	
Amount representing imputed interest	(190,545)	
Present value of future minimum lease payments	$200,644	

Minimum noncancelable sublease rentals to be received in the future, which are not included above as offsets to future payments, total $18,591,000 for capital leases and $19,802,000 for operating leases.

Rent expense on operating leases, including leases relating to business units to be divested and other assets held for sale, in the five months ended December 31, 1987, the seven months ended July 31, 1987, and the years ended December 31, 1986 and 1985, totaled $72,184,000, $83,662,000, $137,712,000 and $125,261,000, including contingent rentals of $5,083,000, $4,881,000, $10,407,000 and $10,022,000, but reduced by sublease rentals of $2,051,000, $2,898,000, $4,004,000 and $3,878,000.

17. *LEASES AND CONTINGENCIES (Continued):*

Contingent rent expense on capital leases, including leases relating to business units to be divested and other assets held for sale, in the five months ended December 31, 1987, the seven months ended July 31, 1987, and the years ended December 31, 1986 and 1985, was $2,776,000, $3,057,000, $6,146,000 and $5,972,000. Contingent rentals are generally based upon sales levels or changes in the Consumer Price Index.

The Company is a defendant in various lawsuits arising in the normal course of business and as a result of the Tender and the Merger. Management believes the ultimate outcome of these lawsuits will not be material to the financial position of the Company.

18. *INTEREST EXPENSE:*

The components of interest expense are as follows:

	Successor	Predecessor		
	Five months ended December 31, 1987	Seven months ended July 31, 1987	Year ended December 31 1986	1985
		(Dollars in thousands)		
Interest on debt	$141,712	$ 45,979	$ 56,178	$ 49,375
Amortization of deferred debt issuance costs	23,002	—	—	—
Interest on capital lease obligations	9,489	12,399	19,034	18,479
Capitalized interest	(10,688)	(13,297)	(17,921)	(11,325)
	$163,515	$ 45,081	$ 57,291	$ 56,529

19. *INCOME TAXES:*

Provisions for income taxes are as follows:

	Successor	Predecessor		
	Five months ended December 31, 1987	Seven months ended July 31, 1987	Year ended December 31 1986	1985
		(Dollars in thousands)		
Currently payable (refundable):				
Federal	$ (54,817)	$ 31,387	$ 33,495	$ 67,980
Canadian	484	2,621	2,843	2,107
State	(6,947)	6,100	11,049	2,400
	(61,280)	40,108	47,387	72,487
Deferred (benefit)	(10,505)	2,758	(1,887)	(2,771)
	(71,785)	42,866	45,500	69,716
Less amounts allocated to business units to be divested at the statutory rate	—	11,456	21,009	15,395
	$(71,785)	$ 31,410	$ 24,491	$ 54,321

19. *INCOME TAXES (Continued):*

Reconciliations of the Company's effective tax rate and the federal statutory rate are as follows:

	Successor	Predecessor		
	Five months ended December 31, 1987	Seven months ended July 31, 1987	Year ended December 31 1986	1985
Federal statutory rate	(40.0)%	40.0 %	46.0 %	46.0 %
Investment tax credits	.5	.6	(1.6)	(5.5)
State income taxes, net of federal income tax benefit	(1.8)	2.8	2.4	.5
Depreciation	—	—	(9.2)	(12.5)
Earnings taxed as dividends	(.6)	(9.2)	(6.3)	(3.2)
Capital gains	—	(2.1)	(13.3)	2.0
Loss to be carried forward	3.7	—	—	—
Amortization of cost in excess of tax basis	6.3	—	—	—
Other	(.5)	.1	.5	(2.6)
	(32.4)%	32.2 %	18.5 %	24.7 %

The provisions for deferred income taxes (benefits) are as follows:

	Successor	Predecessor		
	Five months ended December 31, 1987	Seven months ended July 31, 1987	Year ended December 31 1986	1985
		(Dollars in thousands)		
Use of accelerated depreciation for tax purposes	$ (1,238)	$ 2,788	$ 26,358	$ 42,529
Insurance accruals not deductible for tax purposes	3,394	(7,053)	(13,567)	(20,002)
Write-down of inventories to market not deductible for tax purposes	(1,365)	3,229	(16,142)	(17,480)
Accrued loss on foreign exchange differential	(5,717)	—	—	—
Other	(5,579)	3,794	1,464	(7,818)
	$(10,505)	$ 2,758	$ (1,887)	$ (2,771)

Deferred federal income taxes of $52,511,000 at December 31, 1986, are included in deferred credits and other liabilities. Net deferred tax benefits of $17,434,000 at December 31, 1986, are included in deposits and prepaid expenses.

On October 22, 1986, the Tax Reform Act of 1986 substantially revised the Internal Revenue Code. While most of the provisions of this act were not effective until 1987, the investment tax

19. *INCOME TAXES (Continued):*

credit provision of the existing law was repealed, subject to certain transition rules, effective January 1, 1986.

At December 31, 1987, the Company had a net operating loss carryforward of approximately $20,000,000 for financial statement purposes.

The Company has not yet determined the date or method of future adoption of Statement of Financial Accounting Standards No. 96, "Accounting for Income Taxes." Therefore, the effects of such compliance are not presently determinable.

20. *EARNINGS (LOSS) PER COMMON SHARE:*

Primary earnings (loss) per common share are based on net earnings (loss) applicable to common shares reduced by preferred stock dividends and, subsequent to December 15, 1987, accretion to redemption value of the Redeemable Preferred and the Warrants, divided by the average number of shares, including the Warrants (unless the effect of considering the Warrants is antidilutive), outstanding during each year. Earnings (loss) per share assuming full dilution are based on net earnings (loss) applicable to common shares divided by the sum of (a) shares used in computing primary earnings per share, (b) average shares issuable upon conversion of preferred stock and the Redeemable Preferred (related dividend requirements eliminated), (c) shares issuable upon conversion of convertible debentures at the stated conversion rates (related interest requirements eliminated), (d) shares issuable on the exercise of stock options after reduction for shares assumed to have been purchased with the proceeds and (e) average shares issuable under the Key Employees Incentive Plan.

Earnings (loss) per share of the Predecessor and Successor are computed based upon the relevant number of shares before and after the Merger, respectively. The approximately one-third minority interest from August 1, 1987 to December 31, 1987, is calculated as one-third of the ultimate shares outstanding after the Merger, as the number of Predecessor shares outstanding at that time is not relevant for subsequent periods.

21. *RELATED PARTY TRANSACTIONS:*

Leases With Profit Sharing

At December 31, 1987, Profit Sharing owned 725 stores leased to the Company under capital leases and 759 stores leased to the Company under operating leases at rentals approximating market rates at the date of lease. No stores were purchased from the Company during 1987, 1986 or 1985, although 132 stores were purchased from a third party during 1987. Included in the financial statements are the following amounts related to these leases:

	December 31	
	1987 (Successor)	1986 (Predecessor)
	(Dollars in thousands)	
Buildings, net of accumulated amortization of $34,757 and $34,112	$22,611	$26,517
Capital lease obligations, net of current portion of $3,185 and $3,128	$30,262	$34,798

21. *RELATED PARTY TRANSACTIONS (Continued):*

Leases With Profit Sharing (Continued)

	Successor	Predecessor		
	Five months ended December 31, 1987	Seven months ended July 31, 1987	Year ended December 31 1986	1985
		(Dollars in thousands)		
Rent expense under operating leases and amortization of capital lease assets, including business units to be divested and other assets held for sale, included in cost of goods sold	$14,917	$17,751	$30,094	$30,256
Imputed interest expense on capital lease obligations, including business units to be divested and other assets held for sale	$ 1,779	$ 1,658	$ 3,683	$ 4,080

Transactions With Citgo

Investment in and advances to Citgo are as follows:

	December 31 1987 (Successor)	1986 (Predecessor)
	(Dollars in thousands)	
Interest-bearing advances to Citgo	$ —	$ 100,000
Investment in Citgo	380,037	186,584
Investment in and advances to Citgo	$ 380,037	$ 286,584

In the normal course of operations, the Company purchases refined products from Citgo and receives reimbursement for administrative services and interest on its advances (fully repaid during 1987) to Citgo.

The amounts of refined product purchases from Citgo were $443,000,000, $615,000,000, $954,000,000 and $1,550,000,000 for the five months ended December 31, 1987, the seven months ended July 31, 1987, and the years ended December 31, 1986 and 1985. The decrease during 1986 resulted primarily from a decline in product prices.

In connection with the sale of 50% of the common stock of Citgo, the Company entered into a 20-year product purchase agreement with Citgo to buy gasoline at market-related prices. Minimum required annual purchases under this agreement are generally the lesser of 750,000,000 gallons or 35% of gasoline purchased by the Company for retail sale.

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

DECEMBER 31, 1987

22. *QUARTERLY FINANCIAL DATA (UNAUDITED):*

Summarized quarterly financial data for 1987 and 1986 is as follows:

Year ended December 31, 1987:

	Predecessor			Successor	
	First quarter	Second quarter	July 1 through July 31	August 1 through September 30	Fourth quarter
	(Dollars in millions, except per-share data)				
Net sales:					
Originally reported	$ 2,090	$ 2,434	$ 790	$ 1,501	$ 1,869
Adjustment for business units to be divested and other assets held for sale	(201)	(248)	—	(159)	—
Adjustment to reflect the Merger	—	—	—	—	—
Restated	1,889	2,186	790	1,342	1,869
Gross profit:					
Originally reported	438	555	176	329	447
Adjustment for business units to be divested and other assets held for sale	(60)	(85)	—	(18)	—
Adjustment to reflect the Merger	—	—	(12)	(11)	—
Restated	378	470	164	300	447
Income taxes (benefit):					
Originally reported	15	26	6	13	(62)
Adjustment for business units to be divested and other assets held for sale	(2)	(6)	—	4	—
Adjustment to reflect the Merger	—	—	(8)	(27)	—
Restated	13	20	(2)	(10)	(62)

22. *QUARTERLY FINANCIAL DATA (UNAUDITED) (Continued):*

Year ended December 31, 1987 (Continued):

	Predecessor			Successor	
	First quarter	Second quarter	July 1 through July 31	August 1 through September 30	Fourth quarter
	(Dollars in millions, except per-share data)				
Net earnings (loss):					
Originally reported	$ 25	$ 48	$ 17	$ 33	$ (129)
Adjustment for business units to be divested and other assets held for sale	—	—	—	2	—
Adjustment to reflect the Merger	—	—	—	(56)	—
Restated	25	48	17	(21)	(129)
Primary earnings (loss) per common share:					
Originally reported	.47	.93	.32	.64	(.64)
Adjustment for business units to be divested and other assets held for sale	—	—	—	.01	—
Adjustment to reflect the Merger	—	—	.02	(.76)	—
Restated	.47	.93	.34	(.11)	(.64)
Fully diluted earnings (loss) per common share:					
Originally reported	.47	.92	.31	.64	(.64)
Adjustment for business units to be divested and other assets held for sale	—	—	—	.01	—
Adjustment to reflect the Merger	—	—	.03	(.76)	—
Restated	.47	.92	.34	(.11)	(.64)

22. *QUARTERLY FINANCIAL DATA (UNAUDITED) (Continued):*

Year ended December 31, 1986 (Predecessor):

	First quarter	Second quarter	Third quarter	Fourth quarter	Year
		(Dollars in millions, except per-share data)			
Net sales:					
Originally reported	$ 1,999	$ 2,205	$ 2,269	$ 2,105	$ 8,578
Adjustment for business units to be divested	(175)	(210)	(217)	(193)	(795)
Restated	1,824	1,995	2,052	1,912	7,783
Gross profit:					
Originally reported	455	525	541	454	1,975
Adjustment for business units to be divested	(58)	(72)	(72)	(62)	(264)
Restated	397	453	469	392	1,711
Income taxes (benefit):					
Originally reported	(18)	16	36	12	46
Adjustment for business units to be divested	(4)	(8)	(6)	(4)	(22)
Restated	(22)	8	30	8	24
Net earnings (loss)	(89)	81	184	24	200
Primary earnings (loss) per common share	(1.91)	1.64	3.76	.44	3.96
Fully diluted earnings (loss) per common share	(1.91)	1.59	3.58	.44	3.91

The adjustment to reflect the Merger restates previously reported quarterly financial data for the third quarter of 1987 for the effect of the acquisition of approximately two-thirds of the common stock of the Company by JT on August 1, 1987, and the push-down of JT's August 1 debt and related costs and interest expense to the accounts of the Company.

The fourth quarter of 1987 includes nonrecurring expenses, including $46,100,000 to redeem all outstanding stock options as a result of the Merger and $55,500,000 relating to the unhedging of currency exchange agreements.

22. *QUARTERLY FINANCIAL DATA (UNAUDITED) (Continued):*

The effective tax rate for the fourth quarter of 1986 was 33.4%, which adjusted income tax expense to the actual annual effective tax rate of 18.5% from the previously estimated effective rate of 16.0%. The fourth quarter 1986 tax rate reflects changes as a result of the Tax Reform Act of 1986 (see Note 19).

The third quarter of 1986 included a $99,700,000 pretax gain on the sale of one-half of Citgo's equity. The fourth quarter of 1986 included the recognition of an additional pretax gain of $3,600,000, primarily representing a portion of the deferred gain on the sale recorded at September 30, 1986. During the first quarter of 1987, the remaining pretax gain of $20,900,000 was recognized.

The first and second quarters of 1986 included noncash write-downs to market value of Citgo crude oil and wholesale refined product inventories of $100,000,000 and $54,000,000, pretax, on a FIFO basis for crude oil, at Southland's 100% equity share. During the fourth quarter of 1986, Citgo changed its method of accounting for crude oil from FIFO to LIFO, which increased the 1986 inventory write-downs and Citgo's operating profits by an equal amount, with no effect on net income of Citgo or reported net income of the Company. On a LIFO basis, the write-downs for the first and second quarters of 1986 were $155,000,000 and $67,000,000, pretax. During the fourth quarter of 1986, Citgo recovered part of the write-downs to market, and the Company realized a recovery of $53,000,000 pretax, or $28,000,000 net of Citgo's income tax effect, representing its 50% equity share of Citgo's recovery.

23. *SUBSEQUENT EVENTS:*

Subsequent to December 31, 1987, the Company sold other assets held for sale for approximately $125,000,000 cash, and has contracts in various stages of completion for the sale of business units to be divested and other assets held for sale for approximately $600,000,000 cash. These contracts are subject to certain conditions, and there can be no assurance that the transactions will be consummated.

Item 9. *DISAGREEMENTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.*

During the 24 months prior to December 31, 1987, there was no change of accountants and no reportable disagreement on accounting practices or principles.

PART III

Item 10. *DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.*

The names, ages and positions and offices with the registrant of all current executive officers of the Company are shown in the following chart. John P. Thompson, Jere W. Thompson, and Joe C. (Jodie) Thompson, Jr. (formerly an executive officer and currently a director) are brothers and are the directors of the Company. The term of office of each executive officer is at the pleasure of the board of directors and/or the officer to whom such individual reports. The business experience of each such executive officer for at least the last five years, and the period during which he served in his office, as well as the date each was employed by the Company, are reflected in the applicable footnotes to the chart.

Name	Age at 3/28/88	Current Positions and Offices with Registrant
John P. Thompson	62	Director; Chairman of the Board(1)
Jere W. Thompson	56	Director; President and Chief Executive Officer(2)
Joe C. (Jodie) Thompson, Jr.	47	Director of the Company; President and Chief Executive Officer, Sigel Liquor Stores(3)
S. R. Dole	50	Executive Vice President, 7-Eleven Stores(4)
Walton Grayson, III	59	Executive Vice President, Administration and Services(5)
Clark J. Matthews, II	51	Executive Vice President and Chief Financial Officer(6)
Frank J. Gangi	47	Senior Vice President, Finance(7)
John H. Rodgers	44	Senior Vice President, General Counsel and Secretary(8)
Dale H. Allardyce	38	Vice President, Distribution(9)
John F. Antioco	38	Vice President, Marketing, 7-Eleven Stores(10)
Robert E. Bailey	45	Vice President, Southern Region, 7-Eleven Stores(11)
C. O. Beshears	61	Vice President, Dairies Group(12)
Donald L. Burnside	52	Vice President, Administration, Retail(13)
Adrian O. Evans	51	Vice President, Mid-America Region, 7-Eleven Stores(14)
David M. Finley	47	Vice President, Human Resources(15)
David L. Karney	43	Vice President, Management Information Services(16)
Stephen B. Krumholz	38	Vice President, Northwest Region, 7-Eleven Stores(17)
Stephen B. LeRoy	35	Vice President, Chesapeake Region, 7-Eleven Stores(18)
Hugh G. Robinson	55	Vice President, Cityplace Project (19)
Michael K. Roemer	39	Vice President, Northeast Region, 7-Eleven Stores(20)
Kenneth M. Slauth	51	Vice President, Development(21)
Henry T. Stanley, Jr.	51	Vice President, Corporate Communications(22)
Mitchel E. Telson	45	Vice President, Western Region, 7-Eleven Stores(23)
Richard A. Turchi	53	Vice President, International Operations(24)
Vernon P. Lotman	48	Controller(25)
David A. Urbel	46	Treasurer(26)

(1) Director since 1948; Chairman of the Board since 1969; Chief Executive Officer from 1969 to 1986; President from 1961 to 1969. Employee of the Company since 1948. John Thompson is also a director of First RepublicBank Corporation, IRT Corporation and Texstyrene Corporation.

(2) Director since 1961; President since 1973; Chief Executive Officer since 1986; Executive Vice President, Stores Group and Dairies Group from 1962 to 1973. Employee of the Company since 1956. Jere Thompson is also a director of MCorp and Texstyrene Corporation.

(3) Director of the Company since 1979; President and Chief Executive Officer, Sigel Liquor Stores, Inc. since 1987; Senior Executive Vice President, Retail, of the Company from 1983 to 1986; Executive Vice President, Retail, from 1980 to 1983; Vice President from 1977 to 1980; Central Stores Regional Manager from 1973 to 1978. Employee of the Company from 1971 to 1987.

(4) Executive Vice President, Stores Group and/or 7-Eleven Stores Group since 1985; Senior Vice President, Stores Group from 1980 to 1985; Vice President, Stores Group from 1977 to 1980; Vice President, Company Franchised Convenience Stores, and Northern Stores Regional Manager from 1974 to 1977; Western Stores Division Manager from 1970 to 1974. Employee of the Company since 1964 and of an acquired company since 1957.

(5) Director from 1962 until 1987; Executive Vice President, Administration and Services since 1972. Employee of the Company since 1962.

(6) Director from 1981 until 1987; Executive Vice President and Chief Financial Officer since 1987 and from 1979 to 1983; Senior Executive Vice President and Chief Financial Officer from 1983 until 1987; Vice President and General Counsel from 1973 to 1979. Employee of the Company since 1965.

(7) Senior Vice President, Finance since 1987; Vice President from 1983, and Treasurer from 1980, to 1987. Employee of the Company since 1973.

(8) Senior Vice President, General Counsel and Secretary since 1987; Vice President and General Counsel from 1980 to 1987. Employee of the Company since 1973.

(9) Vice President, Distribution since 1987; Distribution Group Manager from 1986 to 1987; Division Manager, Southern California Distribution Center from May 1986 to October 1986; Division Manager, Midwest Distribution Center from 1984 to 1986; Assistant Division Manager, Orlando Distribution Center from 1982 to 1984. Employee of the Company since 1982.

(10) Vice President, Marketing, 7-Eleven Stores since 1987; Vice President, Marketing-Retail from 1986 to 1987; National Marketing Manager from 1984 to 1986; Division Manager, Northeastern Stores Division from 1980 to 1984. Employee of the Company since 1970.

(11) Vice President, Southern Region, 7-Eleven Stores since 1987; Vice President, Southwestern Stores Region from 1986 to 1987; Regional Manager, Southwestern Stores Region in 1986; Division Manager, Capitol Stores Division from 1982 to 1986; Division Manager, Midwest Stores Division from 1981 to 1982. Employee of the Company since 1970.

(12) Vice President, Dairies Group since 1980; Assistant to Vice President, Dairies Group from 1979 to 1980. Employee of the Company from 1958 to 1973 and since 1975.

(13) Vice President, Administration, Retail since 1987; Vice President, Western Stores Region from 1980 until 1987. Employee of the Company since 1965.

(14) Vice President, Mid-America Region, 7-Eleven Stores since 1987; Vice President, Central Stores Region from 1980 until 1987. Employee of the Company from 1962 until 1972 and since 1975.

(15) Vice President, Human Resources since 1987; Manager, Stores Human Resources in 1987; Manager, Organizational Research and Development from 1982 to 1987. Employee of the Company since 1977.

(16) Vice President, Management Information Services since 1985; Manager, Management Information Services from 1984 to 1985; Manager, Management Information Resource Planning from 1983 to 1984; Manager of Technical Services, The Williams Companies from 1978 to 1983. Employee of the Company since 1983.

(17) Vice President, Northwest Region, 7-Eleven Stores since 1987; Division Manager, Mountain Division, 7-Eleven Stores, from 1986 to 1987; Regional Marketing Manager from 1981 to 1986. Employee of the Company since 1972.

(18) Vice President, Chesapeake Region, 7-Eleven Stores since 1987; Regional Manager, Chesapeake Stores Region in 1987; Division Manager, Capitol Stores Division from 1986 to 1987; Division Manager, Great Lakes Stores Division from 1984 to 1986; Operations Manager, Great Lakes Stores Division from 1981 to 1984. Employee of the Company since 1975.

(19) Vice President, Cityplace Project, and President, Cityplace Development Corporation since 1983; Major General, U.S. Army Corps of Engineers, Division Commander, Southwest Division from 1980 to 1983; Brigadier General, U.S. Army Corps of Engineers, Deputy Director, Civil Works, Office of Civil Engineers from 1978 to 1980. Employee of the Company since 1983.

(20) Vice President, Northeast Region, 7-Eleven Stores since 1987; Division Manager, Northeast Stores Region from 1984 to 1987; Citgo Petroleum Corporation-Vice President, Retail Marketing from 1983 to 1984; Marketing Manager, Eastern Stores Region from 1981 to 1983. Employee of the Company since 1966.

(21) Vice President, Development since 1985; Manager, Development from 1984 to 1985; National Marketing Manager from 1981 to 1984; Division Manager, South Pacific Division from 1978 to 1981. Employee of the Company since 1960.

(22) Vice President, Corporate Communications since 1986; Vice President, Investor Relations from 1982 to 1986. Employee of the Company since 1981.

(23) Vice President, Western Region, 7-Eleven Stores since 1987; Regional Manager, Western Stores Region in 1987; Division Manager, South Pacific Stores Division from 1985 to 1987; Operations Manager, North Texas Stores Division in 1984; General Manager, Chief Auto Parts Division, from 1981 to 1984. Employee of the Company since 1967.

(24) Vice President, International Operations since 1980; Manager, International Department from 1976 to 1980. Employee of the Company since 1963.

(25) Controller since 1987; Assistant Corporate Controller from 1977 to 1987. Employee of the Company since 1973.

(26) Treasurer since 1987; Deputy Treasurer from 1984 to 1987; Assistant Treasurer from 1983 to 1984. Employee of the Company since 1970.

The names, ages, positions and offices formerly held with the registrant and the business experience for at least the past five years of all persons who served as executive officers of the Company during 1987 but who no longer serve as such, are shown below. Also shown for each such person is the period during which he served in his office, as reflected in the footnotes to the following chart.

Name	Age at 3/28/88
James W. Parker(1)	49
Kenneth J. Hughes(2)	44
Frank L. Kitchen(3)	51
P. Eugene Pender(4)	57
L. Mark Rigg(5)	54
R G Smith(6)	65

(1) Executive Vice President, Manufacturing and Distribution from 1983 to 1987; Senior Vice President, Manufacturing and Distribution from 1980 to 1983; Vice President, Dairies Group, 1980; General Manager, Dairies Group from 1978 to 1980; Division Manager, Embassy Dairy Division from 1974 to 1978. Employee of the Company from 1970 until his resignation as an employee in February 1988.

(2) Vice President, Special Operations from 1986 to 1988; General Manager, Special Operations from 1984 to 1986; Division Manager, Fast Foods from 1983 to 1984; Division Manager, Chemical Division from 1981 to 1984. Employee of the Company since 1977.

(3) Vice President, Eastern Stores Region from 1980 to 1987. Employee of the Company since 1960.

(4) Vice President and Controller from 1980 to 1987. Employee of the Company since 1971 and of an acquired company since 1950.

(5) Vice President, Human Resources from 1980 to 1987. Employee of the Company since 1969.

(6) Secretary from 1971 to 1987; Secretary and Treasurer from 1972 to 1980. Employee of the Company since 1951.

Item 11. ***EXECUTIVE COMPENSATION.***

During 1987, the compensation for services of each non-employee director was $30,000 a year, paid $2,500 per month for each month (following election as a director) during which the director served, plus $1,000 for attendance at each regular or special meeting of the Board of Directors or committees thereof. Directors who served as chairmen of the regular committees of the Board of Directors received additional quarterly compensation for such service. Employee directors did not receive additional compensation for their service as directors.

During 1987 there were eight non-employee directors, as follows: William W. Atwell (served from 1976 to 1987), J. Y. Ballard (served from 1937 until his death on June 22, 1987), Frank L. Carney (served from 1982 to 1987), Mark L. Lemmon, M.D. (served from 1977 to 1987), Leo E. Linbeck, Jr. (served from 1982 to 1987), Walter M. Mischer, Jr. (served from 1982 to 1987), Alan C. Schoellkopf (served from 1979 to 1987), and Joe C. (Jodie) Thompson, Jr. (served from 1979 until present). Pursuant to the Merger Agreement, the directors of JT Acquisition became the initial directors of the Company at the effective time of the Merger and the terms of all other directors terminated at that time.

Following the Merger there is no standard arrangement for compensation of directors.

Cash Compensation

The following table sets forth all cash compensation paid or accrued by the Company in 1987 for services in all capacities to each of the five most highly compensated executive officers and to all executive officers as a group.

CASH COMPENSATION TABLE

Name of Individual or Number of Persons in Group	Principal Capacities in Which Served	Cash Compensation(a)
John P. Thompson	Director; Chairman of the Board	$ 735,583
Jere W. Thompson	Director; President and Chief Executive Officer	$ 732,250
Clark J. Matthews, II	Director; Executive Vice President and Chief Financial Officer	$ 419,375
James W. Parker	(Former) Executive Vice President, Manufacturing and Distribution	$ 350,752(b)
S. R. (Dick) Dole	Executive Vice President, 7-Eleven Stores	$ 334,375
All executive officers as a group (31 persons)(c)		$7,417,542

(a) Includes base salary and all cash bonuses paid to, or accrued for, the named individuals and the group for services rendered to Southland in all capacities during 1987, including the portion of

bonuses paid in 1988 for services rendered in 1987 and including any amounts which would have been paid for services rendered in 1987 but the payment of such compensation was deferred. The amount paid to any employee under the Company's bonus plan is based upon a percentage of the employee's base salary and the satisfaction of certain performance criteria by the Company and/or the employee's operating division. Cash compensation paid pursuant to other Company plans is not included in this table but is shown on the following pages where each plan is described.

(b) Mr. Parker resigned as an officer of the Company effective August 7, 1987. The Company entered into an agreement with him concerning his performance of services in connection with his resignation as an officer pursuant to which he was paid an additional $155,000 in 1987, not included in this table.

(c) Amounts in this table and in all following tables include compensation paid for the full year to officers who did not serve for the full year and are not allocated solely for the time during which they served as officers.

COMPENSATION PURSUANT TO PLANS

Executive Protection Plan

The Executive Protection Plan, established in 1974, provides officers and certain other employees with retirement, disability and pre-retirement death benefits in addition to the Company's group plans. Benefits under this Plan are adjusted each July 1, and may be changed or cancelled by the Company at any time. The Company has purchased individual life insurance policies which, over time, are expected to reimburse the Company for its expenses under the Plan.

Retirement benefits (the salary continuation portion of the Plan) are payable in equal installments over 10 years and, effective July 1, 1984, the Plan was amended to provide that such benefits would be based upon one and one-half times the actual base salary and normal bonus (excluding amounts received under any other benefit plan) earned by the individual from the Company for the calendar year prior to retirement. Normal retirement is at age 65. In the event of early retirement, which is permitted at age 55, benefits are reduced 5% for each year before normal retirement age.

Disability benefits are payable monthly, based on 80% of the participant's actual base salary plus normal bonus from the Company for the calendar year preceding the disability, and continue until death or retirement. The amounts include a 75% benefit for the first 26 weeks under the Company's Group Disability Plan (which was increased, in 1985, from 65%) and a 65% benefit thereafter under that plan, based on the participant's actual base salary and normal bonus from the Company for the calendar year preceding the effective date of the coverage in force when the disability occurs.

Pre-retirement death benefits are payable in 10 equal annual payments and are based upon twice the actual base salary and normal bonus earned by the individual from the Company for the prior calendar year, excluding amounts received under any other benefit plan.

The following table sets forth the amounts expensed by the Company, including premiums paid, net of increase in cash surrender value and policy loans, as well as any accruals to cover the increase in the Company's actuarially determined present value liability under the salary continuation portion of the Plan, in 1987, for each of the named individuals and for all officers as a group.

Name of Individual or Number of Persons in Group	Executive Protection Plan
John P. Thompson	$ 48,866
Jere W. Thompson	124,301
Clark J. Matthews, II	33,458
James W. Parker(a)	(80,445)
S. R. (Dick) Dole	44,234
All eligible officers as a group (31 persons)	$ 382,858

(a) Due to the fact that Mr. Parker resigned in 1987 and the Company has no future liability for benefits to him under the Plan, the Company experienced an income effect in 1987 essentially equal to the difference between -0- liability in 1987 and the approximately $81,000 liability in 1986.

The following table sets forth the additional benefits presently provided under the Executive Protection Plan for each of the named individuals and for all eligible officers as a group.

Name of Individual or Number of Persons in Group	Total Retirement Benefits	Monthly Additional Disability Benefits Before Retirement	Total Pre-Retirement Death Benefits
John P. Thompson	$ 1,431,265	$ 63,612	$ -0- (a)
Jere W. Thompson	1,484,670	65,985	-0- (a)
Clark J. Matthews, II	745,594	33,138	-0- (a)
James W. Parker	464,980(b)	20,666(b)	619,974(b)
S. R. (Dick) Dole	447,543	19,891	596,724
All eligible officers as a group (31 persons)	$10,877,814(b)	$483,462(b)	$ 9,190,443(b)

(a) Those employees who served as directors in 1987 were covered under the Split Dollar Life Insurance Program in lieu of receiving pre-retirement death benefits under the Executive Protection Plan.

(b) Amounts shown include benefits payable to officers who resigned or retired during 1987 and the first three months of 1988 although the benefits may have been terminated at the time of such resignation or retirement.

Post Retirement Life Insurance

The Company also provides post retirement life insurance to all officers and certain other employees. Upon retirement, the Company will provide the retiree with a life insurance policy with a face value upon death of approximately two times the retiree's base salary and normal bonus from the Company during his final year of employment. This Plan was instituted during 1984 to replace the terminated Retired Lives Reserve. Under this Plan, the Company purchases policies to provide this insurance. Premiums will be paid by the Company for the first seven years, at which time it is anticipated the earnings on the policies will be sufficient to pay all premiums as well as reimburse the Company for all its expenses, including interest on the premiums paid.

The following table sets forth the amounts expensed by the Company, including premiums paid, net of increase in cash surrender value and policy loans, under the Post Retirement Life Insurance Plan in 1987, as well as the total amount of insurance to be provided for each of the named individuals and all officers as a group.

Name of Individual or Number of Persons in Group	Total Insurance Provided	Post Retirement Expense(a)
John P. Thompson	$ 2,203,354	$(10,565)
Jere W. Thompson	2,279,560	(8,058)
Clark J. Matthews, II	1,009,126	(1,960)
James W. Parker	919,974(b)	(1,998)(b)
S. R. (Dick) Dole	611,724	(1,248)
All eligible officers as a group (31 persons)	$15,725,732(b)	$ (1,426)(b)

(a) Represents increase in cash surrender value. All premiums were paid through policy loans.

(b) Amounts shown include benefits payable to officers who resigned or retired during 1987 and the first three months of 1988 although the benefits may have been terminated at the time of such resignation or retirement.

Split Dollar Life Insurance

The Split Dollar Life Insurance Program, which was instituted in 1981, was provided for both employee and non-employee directors of the Company who had not reached 65 years of age. Premiums were paid by the Company for the first four years. From the fourth until the seventh year

the policies provide that premiums are to be paid through a loan against the policy. Under the program, the director owned only the death benefit portion of the policy until the seventh year at which time the Company would be reimbursed from the policy for all its expenses, including interest on the premiums paid. Following the Merger, the Company has maintained these policies for the current directors as well as those whose terms ended as a result of the Merger and, when such policies are fully paid, the Company intends to provide various alternatives to the directors and former directors in connection with disposition of the policies.

The following table sets forth the total death benefits payable under the policy for the named directors and for all eligible directors as a group. In 1987 the entire $469,460 of premiums due was paid through policy loans.

Name of Individual or Number of Persons in Group	Total Death Benefit
John P. Thompson	$1,396,000
Jere W. Thompson	1,346,000
Clark J. Matthews, II	822,000
All eligible directors as a group (11 persons)	$8,184,000

Employees' Savings and Profit Sharing Plan

The Company also provides The Southland Corporation Employees' Savings and Profit Sharing Plan ("Profit Sharing") as a retirement benefit for eligible employees. Participants defer 6% of their compensation (the maximum deferral was $7,000 for 1987 and is $7,313 for 1988 as determined in accordance with Profit Sharing and Internal Revenue Service regulations), and the Company makes an annual contribution of the greater of 10% of its net earnings before contributions to Profit Sharing and federal income taxes or any amount authorized by the Company's Board of Directors. The Company contribution is allocated to participants on the basis of their current year deferrals, years of participation in Profit Sharing and age, although certain anti-discrimination tests mandated by the 1986 Tax Reform Act had the effect in 1987, and may continue to require, a reduction in the amount that may be deferred by certain participants and/or allocated to their accounts as Company contribution. A participant's deferrals, increased by Profit Sharing's earnings or decreased by Profit Sharing's losses thereon, are always fully vested in the participant and may be withdrawn at any time with the approval of the trustees and pursuant to the terms of Profit Sharing and any applicable laws or regulations. Company contributions, Profit Sharing's earnings and losses thereon and lapses, vest in a participant over the first five years of participation. Thereafter a participant is fully vested in all such amounts. Benefits are payable on retirement, separation from service or death, in a lump sum or in installments as determined by the trustees. Profit Sharing is administered by the trustees, who are appointed by the Board of Directors. The present trustees are Messrs. John Thompson and S. R. Dole (see "Executive Compensation"), John Rodgers (Senior Vice President, General Counsel and Secretary) and Ms. Margaret Fuller (Plan Administrator). Trustees receive no compensation for their services as trustees.

The following table sets forth for each of the named individuals and all eligible officers as a group the amounts allocated to their accounts as Company contribution in 1987.

	John P. Thompson	Jere W. Thompson	Clark J. Matthews, II	James W. Parker	S.R. (Dick) Dole	All eligible officers as a group (31 persons)
Company Contribution.	$11,215	$11,215	$11,215	$8,411	$11,215	$279,530(a)

(a) This amount includes non-vested, as well as vested, Company contribution to the accounts of two officers.

Employee Stock Ownership Plan

Effective January 1, 1983, the Company adopted the ESOP for eligible employees. Contributions to the ESOP were made by the Company in shares of Common Stock limited to .5% of the aggregate compensation of the participants. The Company contribution was allocated to all the participants on an equal basis. The Company terminated the ESOP in 1987 due to changes in the tax laws and made no additional contribution to the plan for 1987.

Key Employees Incentive Plan

Prior to the Merger, the Company maintained the Key Employees Incentive Plan which provided for annual incentive awards to certain key employees predicated upon increased before-tax profits of the Company. Approximately 70% of the awards were payable in Common Stock and the balance in cash to Profit Sharing as deferrals by participants and to the Internal Revenue Service as withholding tax for participants. No awards were made under this plan for 1987 and it has now been terminated.

Executive Interest Differential Program

The Executive Interest Differential Program currently provides for the Company to reimburse officers and other eligible employees a portion of the interest they pay on mortgage loans for their principal residences and for other personal purposes. The Company will reimburse the difference in interest between the actual amortization schedule and one computed on an interest rate 5% lower, but only to the extent that such lower interest rate is 7% or more. The maximum principal amount on which the interest differential will be paid is two and one-half times the individual's annual base salary on a mortgage loan for the principal residence and, for personal loans, in the aggregate one times the individual's annual base salary. This program has been limited as of January 1, 1988 so that no new loans may be added to those on which reimbursement was then being received, except in the case of home mortgage loans where the effect is the same or less reimbursement to the employee. In addition, as of June 30, 1988, no personal loans (i.e., non-mortgage loans) will be covered under the program.

The following table sets forth the amounts paid in 1987 as interest differential to each of the named individuals and to all officers as a group.

	John P. Thompson	Jere W. Thompson	Clark J. Matthews, II	James W. Parker	S.R. (Dick) Dole	All officers as a group (28 persons)
Interest Differential ...	$15,184	$ -0-	$13,080	$9,644	$13,894	$230,860

Tax Preparation

All officers are provided the opportunity to have their income tax returns prepared by, and receive tax planning advice from, Touche Ross & Co., the Company's auditors, at the Company's expense. In 1987, the Company paid a total of $88,568 to Touche Ross & Co. for this service, including $9,905 for Mr. Matthews and $13,401 for Mr. Dole, the only named individuals who participated in this Program. A total of 18 officers participated in this Program in 1987. The Company may amend this Program in 1988.

Executive Car Program

Until termination of this plan in 1987, all officers were provided with a Company car. Those officers who had Company cars at the time this plan was terminated are permitted to retain those cars under the original terms of the plan. Use of the car is included as taxable income to them for the year. In addition the plan provides that officers may purchase the cars they had been using for three or more years. The purchase price is the book value of the car and an officer who purchases his car is reported as receiving additional income equal to the difference between the appraised value and book value of the car. For 1988, those officers who do not have a Company car will receive a net payment, after tax, of $1,000 per month from the Company in lieu thereof. In accordance with the federal tax laws, officers' taxable income was increased for 1987 based upon the lease value plus operating costs of their cars and the Company then paid each officer a tax offset amount, in cash, equal to 40% of the total automobile use.

The following table sets forth the amounts included as income resulting from personal use by officers of their Company car, the income attributable for purchase of the car at book value and the amount of tax offset paid under the Program during 1987 to each of the named individuals and to all officers as a group.

	John P. Thompson	Jere W. Thompson	Clark J. Matthews, II	James W. Parker	S.R. (Dick) Dole	All officers as a group (24 persons)
Amount included in Income for Personal Use of Car	$ 3,287	$ 6,166	$ 1,546	$ 3,371	$10,726	$173,992
Difference between Appraised Value and Book Value upon Purchase	N/A	N/A	N/A	$16,600	N/A	$ 38,910
Tax Offset Payment	$ 1,730	$ 2,467	$ 2,473	$ 2,752	$ 4,290	$ 88,107

Other Compensation

The Company's facilities, including apartments, condominiums and aircraft, are available for business use by employees, officers and non-employee directors. During 1987 certain officers and non-employee directors used these facilities for personal purposes and reimbursed the Company for such use based upon a formula which took into consideration the cost to the Company of providing such facilities. The incremental cost to the Company, in excess of the amount reimbursed, was approximately $145,000 during 1987 for seven persons. In addition, nine officers received other benefits (including incentive trips and bonuses) with a total value of approximately $220,000.

Other Future Compensation

The Company has arrangements with all officers and employee directors providing for minimum annual salary in 1988 of an aggregate of $4,692,250 and for additional amounts as incentive compensation. Most of Southland's sales and supervisory personnel also are compensated on some form of incentive basis.

The Company has an employment agreement, through December 31, 1990, with John Thompson which provides for his salary to be fixed annually by the Board of Directors, and for incentive compensation to be determined, as it is for other staff officers, by the Company's performance. His base salary has been set at $505,000 for 1988 with incentive compensation based upon 60% of base salary. The agreement entitles him to receive retirement or death benefits, payable monthly, based on original amounts set forth in the agreement, adjusted pursuant to a formula. The original amount of the death benefit before retirement is $574,960 in 1985, increasing in increments of $20,000 to $31,000 per year to $706,883 in 1990. Disability benefits are calculated pursuant to a formula so that the after-tax cost to the Company will be $875 per month. This amount will be provided under the insurance policy described below and will be in addition to amounts payable under other Company plans. Retirement benefits, beginning in 1991, would be payable monthly from the original amount of $724,161. The original amount of the retirement or death benefit is increased (or decreased) annually, until the adjusted original amount is paid, at the Company's average after-tax rate of return on assets for the year, and is reduced by the after-tax cost to the Company of making the payments. Such amount is paid monthly at the rate of $9,000 (adjusted for changes in the Consumer Price Index). Under the agreement, $20,000 is deducted annually from the incentive compensation to be paid. Part of this amount is used to offset the cost to the Company of maintaining an insurance policy on Mr. Thompson's life to fund these obligations. If employment is terminated prior to 1990, the retirement benefit shall be reduced by an amount determined equitable by the Board of Directors to compensate the Company for the years $20,000 is not so deducted.

The Company established a Deferred Compensation Plan for Officers and Directors during 1982 under which an officer may defer a portion or all of such officer's bonus compensation and a director may defer a portion or all of such director's fees. The Plan was effective for compensation received beginning in 1983 and any amounts deferred by officers have been included in the Cash Compensation Table. Amounts are deferred for at least five years and earn interest of 10% per year, compounded

annually. The officer or director may choose the manner in which payments may be made (i.e., lump sum or installments) and the date when payments will begin so long as the minimum deferral requirements are satisfied. In addition, in certain cases, with specific approval, officers have been permitted to defer portions of their regular base salary with terms similar to those provided under the Plan, or, in some cases to defer a portion of their income to 1988.

It is anticipated that senior management and other key employees of the Company ("Key Employees") will be given the opportunity to participate in the common equity of the Company after the Merger. No definitive decision has been made as to the manner or extent in which Key Employees will participate, although it is intended that up to 15% (or 13.5% assuming dilution from the Warrants) of the Company's common equity will be reserved for issuance to Key Employees either by direct sales, the granting of employee stock options, or other similar arrangements. The Company has expressed an intent to implement a plan pursuant to which the Company would issue to approximately 115 Key Employees following the Merger an aggregate of up to $35 million principal amount of its debentures, which will be convertible into such 15% of the common equity of the Company. The Key Employees would be permitted to pay for the debentures in cash or by delivery of a promissory note in a principal amount equal to the principal amount of the debentures. The definitive terms of the plan and the debentures are still being reviewed by the Company. It is anticipated that such debentures will rank junior to other outstanding debt of the Company.

Options

During 1987 no options were granted under the Employees' Stock Option Plan and, in connection with the Merger, the Plan was terminated effective December 15, 1987, and all outstanding options were cancelled. In accordance with the Plan, each holder of an outstanding option, whether or not then exercisable, was entitled to exercise all options held. The Merger Agreement provided that, as to all options not exercised, the optionee became entitled to receive, from the Company, an amount in cash equal to the excess of the price paid per share of Common Stock in the Merger over the per share exercise price of the option. This amount was paid in 1988. The following table sets forth for each of the named individuals and all officers as a group, the number of shares acquired, between January 1, 1987 and December 15, 1987, through the exercise of options under the Plan and the amount paid in cash to the optionee, if any, upon the exercise of options, during that period as well as the amount paid in 1988 in settlement of the cancellation of all outstanding options. The Plan provided that upon exercise of certain options (the only type of option granted to officers) the Company could make a cash payment to the optionee equal to the difference between market value and exercise price on the date the option is exercised. This amount was also paid in 1988. The purchase price of the Common Stock under each option was the closing price for the Common Stock on the New York Stock Exchange on the last trading day before the option was granted.

Common Stock	John P. Thompson	Jere W. Thompson	Clark J. Matthews, II	James W. Parker	S.R. (Dick) Dole	All officers as a group (31 Persons)
Exercised— January 1, 1987 to December 15, 1987(1)	-0-	-0-	-0-	23,067	-0-	58,188
Amount paid to optionee in cash (market value less exercise price)(2)....	-0-	-0-	-0-	$792,070	-0-	$1,600,066
Amount paid in 1988 upon cancellation of stock options.....	$1,593,750	$1,593,750	$638,375	$575,625	$796,875	$12,972,082
Amount paid in 1988 as tax offset right...	$1,593,750	$1,593,750	$638,375	$575,625	$796,875	$12,948,752

(1) The exercise price under the Plan is, for each option, the closing price for the Common Stock on the New York Stock Exchange on the last trading day before the option is granted.

(2) Equal to net value of securities realized at time of exercise.

The Employees' Stock Option Plan was amended in 1983 to extend the term of the Plan, make it available to a larger number of employees, provide for the granting of incentive stock options, increase the number of shares reserved for options and other conforming changes, all of which were approved by the shareholders. In addition, shareholder approval was obtained to allow the delivery of already-owned shares in exchange for option shares. The Plan was also amended in 1987 to conform with certain provisions of the Tax Reform Act of 1986.

Item 12. *SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.*

Security Ownership of Certain Beneficial Owners

At March 28, 1988, the Company was aware of the following beneficial owners of 5% or more of the Company's shares of Common Stock (the only class of voting security of the Company) as listed below:

Title of class	Name and address of beneficial owner	Amount and nature of beneficial ownership	Percent of class
Common Stock, $.01 par value	The Philp Co.(a)	58,250,000 Shares	29.125%
Common Stock, $.01 par value	Thompson Brothers, L.P.(b)	101,750,000 Shares	50.875%
Common Stock, $.01 par value	The Hayden Company(c)	30,000,000 Shares	15.000%
Common Stock, $.01 par value	The Williamsburg Corporation(d)	10,000,000 Shares	5.000%

The address for all the above owners is c/o The Thompson Company, 100 Crescent Court, Dallas, Texas 75201

(a) The Philp Co.'s voting stock is owned by two trusts of which John, Jere and Joe C. (Jodie) Thompson, Jr., serve as trustees. They also are its executive officers and directors, are brothers and may be "control persons" of the Company within the meaning of that term under the rules and regulations of the Securities and Exchange Commission. For additional information concerning the ownership of the Common Stock by The Philp Co. and John, Jere and Jodie Thompson, see "Security Ownership of Management."

(b) Thompson Brothers, L.P. is a Texas limited partnership in which three Thompson family limited partnerships, each controlled by one of the Thompsons, are the general partners and The Philp Co. is the limited partner.

(c) The Hayden Company is a Texas corporation controlled by John P. Thompson.

(d) The Williamsburg Corporation is a Texas corporation controlled by Jere W. Thompson.

No other person is known by the Company to beneficially own any of the Common Stock.

Security Ownership of Management

Following the Merger, only The Philp Co., Thompson Brothers, L.P., the Hayden Company and The Williamsburg Corporation, all of which are controlled by the Thompson family, own any shares of the Common Stock of the Company, as set forth under "Security Ownership of Certain Beneficial Owners." The following table shows the ownership by the directors (John, Jere and Jodie Thompson), and by all officers as a group, of the 15% Cumulative Exchangeable Preferred Stock, Series One, (the "15% Preferred Stock") of the Company. This is non-voting stock (except in limited circumstances, including if there is default in payment of dividends on the stock).

Name of Beneficial owner	Amount and nature of beneficial ownership	Percent of class(a)
John P. Thompson	858,711(b)	8.66%
Jere W. Thompson	376,146(c)	3.80%
Joe C. (Jodie) Thompson, Jr.	507,901(d)	5.12%
All directors and officers as a group (32 persons)	1,206,322(a)	12.17%

(a) As reported to the Company at February 1, 1988. At February 1, 1988, there were 9,911,647 shares of the 15% Preferred Stock outstanding or eligible to be outstanding if all outstanding

shares of Common Stock had been surrendered for conversion in the Merger. The nature of beneficial ownership of the shares reported, if not direct, is described in this footnote (a) and the footnotes that follow. Included in the numbers of shares shown, as required by the rules and regulations of the Securities and Exchange Commission, are those shares as to which such persons have or share voting and/or investment power, or which they have a right to receive within 60 days including the 29,476 shares issued to all officers and directors as the regular quarterly dividend on the 15% Preferred Stock and the 6,894 issued as the dividend to Profit Sharing, which was paid on March 15, 1988, as well as those shares owned by Profit Sharing. Because of these requirements, 316,920 shares are duplicated under John, Jere and Jodie Thompson. In addition, the total 183,856 shares owned by Profit Sharing are included for John Thompson, one of the trustees who, together with the other trustees, has investment (and voting) power over those shares. These duplications are excluded from the number of shares for all officers and directors as a group.

(b) 357,935 by The Hayden Company (whose voting stock he owns), 316,920 by The Philp Co. (whose voting stock is owned by two trusts of which John, Jere and Jodie Thompson serve as three of the trustees) and 183,856 by Profit Sharing, as to which he is one of the trustees.

(c) 59,226 by The Williamsburg Corporation (whose voting stock he owns) and 316,920 by The Philp Co. (see (b) above).

(d) 190,981 (directly or through brokers) by The Florida Company (whose voting stock he owns) and 316,920 by The Philp Co. (see (b) above).

Item 13. ***CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.***

Profit Sharing did not purchase any store locations from the Company during 1987; however, Profit Sharing did purchase three parcels of land (adjoining existing store locations owned by Profit Sharing) from the Company for an aggregate purchase price of $110,496 and purchased 132 store locations from an unaffiliated party that wished to terminate a prior sale and leaseback transaction. As of December 31, 1987, Profit Sharing owned a total of 1,369 operating stores and 115 other locations which were leased to the Company at rates slightly more favorable to Profit Sharing than contemporaneously available similar transactions with third parties. Rentals, including percentage rents, paid by the Company to Profit Sharing for 1987 aggregated $35,120,066. Profit Sharing sold 35 locations (which were all either closed stores or excess property) to third parties during 1987 and the leases with the Company were terminated upon payment by the Company of $474,338 as termination fees.

John, Jere and Jodie Thompson are three of the trustees of a trust which owns the voting stock of Cherry, S.A. During 1987, the Company paid Cherry, S.A. net rental of $40,860 for the business use of a house.

John, Jere and Jodie Thompson and family interests indirectly own a majority of Nationwide Industries, Inc., (a manufacturer of automobile products) of which Marlenn Corporation is a wholly owned subsidiary. During 1987, the Company purchased, for resale, approximately $885,191 of various products from Nationwide Industries, Inc. and $300,746 from Marlenn Corporation, all in the ordinary course of business.

John, Jere and Jodie Thompson and family interests indirectly own a significant interest in Texstyrene Corporation (of which John Thompson and Jere Thompson are two of the directors). During 1987, the Company purchased approximately $3,124,000 of foam cups and lids from a subsidiary of Texstyrene Corporation. All such purchases were the subject of competitive bids.

Artesia Water Company (a bottler of natural spring water) from which the Company purchased $72,695 of bottled water for resale during 1987, is 40-percent owned by the father of Walter Mischer, Jr., who was a director of the Company in 1987. All such purchases were in the ordinary course of business.

Mr. James W. Parker, formerly Executive Vice President, Manufacturing and Distribution of the Company, resigned as an employee of the Company to become the Chief Executive Officer of MorningStar Foods Inc., which is acquiring the Dairies Group from the Company. The transaction, which is expected to close at the end of March 1988, involves a negotiated price for the fixed assets being purchased, plus additional amounts for inventory, accounts receivable and other items, the total amount of which is still to be determined.

PART IV

Item 14. ***EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K.***

(a) The following documents are filed as a part of this report:

1. The Southland Corporation and Subsidiaries' Financial Statements.

2. The Southland Corporation and Subsidiaries' Financial Statement Schedules, included herein.

Citgo Petroleum Corporation and Subsidiaries' Financial Statements

Citgo Petroleum Corporation and Subsidiaries' Financial Statement Schedules

All other schedules have been omitted because they are not applicable, are not required, or the required information is shown in the financial statements or notes thereto.

3. The following is a list of the Exhibits required to be filed by Item 601 of Regulation S-K.

3.	Articles of Incorporation and Bylaws:	
3.(1)	Restated Articles of Incorporation of The Southland Corporation, as amended through December 21, 1987*.	Tab 1
3.(2)	Bylaws of The Southland Corporation, restated as amended through December 16, 1987*.	Tab 2
4.(i)(1)	Instruments defining the rights of security holders, including indentures (see Exhibits (3).(1) and (3).(2), above).	
4.(i)(2)	Specimen Certificate for Common Stock, \$.01 par value, incorporated by reference to File No. 0-676, Annual Report on Form 10-K for year ended December 31, 1980, Exhibit 4.8, Tab. 2	
4.(i)(3)	Specimen Certificate for 15% Cumulative Exchangeable Preferred Stock, Series One, incorporated by reference to Form 8-A, filed March 24, 1988, Exhibit 1.	
4.(i)(4)	Form of Statement of Resolution Establishing Series of Shares for 15% Cumulative Exchangeable Preferred Stock, Series One, incorporated by reference to Form 8-A, filed March 24, 1988, Exhibit 2.	
4.(i)(5)	Form of Indenture, including Debenture, with Mellon Bank, N.A. as trustee providing for 15% Junior Subordinated Exchange Debentures incorporated by reference to Registration Statement on Form S-4, Reg. No. 33-17940, Exhibit 4.2.	
4.(ii)(1)	Form of Indenture, including Debenture, with Norwest Bank Minneapolis, N.A., as trustee, dated December 15, 1987 providing for 15¾% Senior Subordinated Notes due 1997, incorporated by reference to Amendment 4 to Registration Statement on Form S-3, Reg. No. 33-16822, Exhibit 4.1.	
4.(ii)(2)	Form of Indenture, including Debenture, with Norwest Bank Minneapolis, N.A., as trustee, dated December 15, 1987 providing for 16½% Senior Subordinated Discount Notes due 1997, incorporated by reference to Amendment 4 to Registration Statement on Form S-3, Reg. No. 33-16822, Exhibit 4.2.	
4.(ii)(3)	Form of Indenture, including Debenture, with MBank Dallas, N.A., as trustee, dated December 15, 1987 providing for 16¾% Subordinated Debentures due 2002, incorporated by reference to Amendment 4 to Registration Statement on Form S-3, Reg. No. 33-16822, Exhibit 4.3.	

4.(ii)(4)	Form of Indenture including Debenture, with United States Trust Company of New York as trustee, dated December 15, 1987 providing for 18% Junior Subordinated Discount Debentures due 2007, incorporated by reference to Amendment 4 to Registration Statement on Form S-3, Reg. No. 33-16822, Exhibit 4.4.	
4.(ii)(5)	Warrant Agreement including Form of Warrant between the Company and Norwest Bank Minneapolis, N.A., as Warrant Agent, dated December 15, 1987 providing for 26,135,682 warrants, incorporated by reference to Amendment 4 to Registration Statement on Form S-3, Reg. No. 33-16822, Exhibit 4.5.	
4.(ii)(7)	Indenture among Cityplace Center East Corporation, Security Pacific National Bank, as trustee, and The Sanwa Bank Limited, Dallas Agency, dated as of February 15, 1987, providing for 7⅞% Notes due February 15, 1995, incorporated by reference to File No. 0-676, Annual Report on Form 10-K for the year ended December 31, 1986, Exhibit 4(ii)(8).	
4.(ii)(8)	Specimen 7⅞% Note due February 15, 1995, issued by Cityplace Center East Corporation, incorporated by reference to File No. 0-676, Annual Report on Form 10-K for the year ended December 31, 1986, Exhibit 4(ii)(9).	
4.(ii)(9)	Fiscal Agency Agreement among Southland Canada, Inc., as Issuer, The Southland Corporation, as Guarantor and Orion Royal Bank Limited, as Fiscal and Paying Agent, relating to Can. $50,000,000 12% Guaranteed Notes due 1992.*	Tab 3
9.	Voting Trust Agreement. None.	
10.	Material Contracts	
10.(i)(1)	Agreement and Plan of Merger between the Company and JT Acquisition Corporation dated July 3, 1987, as amended, incorporated by reference to Rule 13e-3 Transaction Statement on Schedule 13E-3 by The Southland Corporation, first filed on July 6, 1987 (the "Schedule 13E-3"), Exhibit (c)(1) and Amendment No. 6 to the Schedule 13E-3, Exhibit (c)(4) and Amendment No. 9 to the Schedule 13E-3, Exhibit (c)(5).	
10.(i)(2)	Stock Purchase Agreement, as amended, dated as of September 15, 1986, among The Southland Corporation, Citgo Petroleum Corporation, Petroleos de Venezuela, S.A. and Propercit S.A., incorporated by reference to File No. 0-676, Form 8-K dated September 30, 1986, Exhibit (2), Tab 1.	

10.(i)(3)	Credit Agreement among the Company, JT Acquisition Corporation and the Banks dated as of July 31, 1987 and Amended and Restated as of November 5, 1987.*	Tab 4
10.(i)(4)	Credit and Reimbursement Agreement by and between Cityplace Center East Corporation, an indirect wholly owned subsidiary of Southland, and The Sanwa Bank Limited, Dallas Agency, dated February 15, 1987, relating to $290 million of 7⅞% Notes due February 15, 1995, issued by Cityplace Center East Corporation (to which Southland is not a party and which is non-recourse to Southland) incorporated by reference to File No. 0-676, Annual Report on Form 10-K for the year ended December 31, 1986, Exhibit 10(i)(6).	
10.(ii)(A)	Uniform Franchise Offering Circular, including 7-Eleven Store Franchise Agreement.*	Tab 5
10.(iii)(A)(1)	John P. Thompson Restated Employment Contract dated December 23, 1983, incorporated by reference to File 0-676, Annual Report on Form 10-K for the year ended December 31, 1983, Exhibit 10(iii)(A)(1), Tab 4.	
10.(iii)(A)(2)	The Southland Corporation Executive Protection Plan, as in effect on December 31, 1983, incorporated by reference to File 0-676, Annual Report on Form 10-K for the year ended December 31, 1980, Exhibit 10(c)-2, Tab 7.	
10.(iii)(A)(3)	The Split Dollar Insurance Plan for Directors, as in effect December 31, 1983, incorporated by reference to File No. 0-676, Annual Report on Form 10-K for the year ended December 31, 1981, Exhibit 10(c)(6), Tab 5.	
10.(iii)(A)(4)	Deferred Compensation Plan, sample agreement, for officers and directors incorporated by reference to File No. 0-676, Annual Report on Form 10-K for the year ended December 31, 1982. Exhibit 10(iii)(A)(7), Tab 2.	
10.(iii)(A)(5)	Executive Company Car Program, sample agreement, incorporated by reference to File No. 0-676, Annual Report on Form 10-K for the year ended December 31, 1982, Exhibit 10(iii)(A)(8), Tab 3.	
10.(iii)(A)(6)	Executive Interest Differential Reimbursement Program, incorporated by reference to File No. 0-676, Annual Report on Form 10-K for the year ended December 31, 1982, Exhibit 10(iii)(A)(9). Tab 4.	
10.(iii)(A)(9)	Bonus Deferral Agreement relating to 1987 Bonus Payment.*	Tab 6

11.	Statement re computation of per-share earnings.	Tab 7
	(a) Calculation of primary earnings per share.*	
	(b) Calculation of earnings per share assuming full dilution.*	
12.	Statements re computation of ratios. None.	
13.	Annual Report to security holders. None.	
18.	Letter re change in accounting principles. None.	
19.	Previously unfiled documents. None.	
22.	Subsidiaries of the Registrant as of January 1, 1988.*	Tab 8
23.	Published report regarding matters submitted to vote of security holders. None.	
24.	Consents of Experts and Counsel.	
	Consent of Touche Ross & Co., Independent Certified Public Accountants.*	Tab 9
25.	Power of Attorney. None.	
28.	Additional Exhibits.	
28.(1)	The Southland Corporation Employees' Savings and Profit Sharing Plan. Form 11-K Annual Report.*	Tab 10
	The Southland Employees' Trust Financial Statements as of December 31, 1987 and 1986 and for each of the three years in the period ended December 31, 1987; to be filed by amendment.	
28.(2)	Employees' Thrift Plan of Citgo Petroleum Corporation. Form 11-K Annual Report.*	Tab 11
	Financial Statements of the Employees' Thrift Plan of Citgo Petroleum Corporation as of December 31, 1987 and 1986 and for each of the three years in the period ended December 31, 1987.*	

*Filed or furnished herewith

(b) Reports on Form 8-K. One report on Form 8-K was filed dated November 20, 1987 (as amended by Form 8, dated November 27, 1987), providing the consolidated balance sheets of The Southland Corporation and subsidiaries as of December 31, 1986, and the related consolidated statements of earnings, shareholders' equity and changes in financial position for each of the three years in the period ended December 31, 1986, and related information, restated to reflect the discontinued operations of certain segments of the business, together with the applicable reports of independent certified public accountants.

In addition, the Company filed a report on Form 8-K, dated February 16, 1988, in connection with a legal proceeding pending in the United States District Court for the Southern District of Florida.

(c) The exhibits required by Item 601 of Regulation S-K are attached hereto or incorporated by reference herein.

(d) (1) The financial statements and financial statement schedules for Citgo Petroleum Corporation and Subsidiaries are attached hereto.

(3) The financial statement schedules for The Southland Corporation and Subsidiaries are attached hereto.

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors and Shareholders
The Southland Corporation
Dallas, Texas

In connection with our examination of the consolidated financial statements of The Southland Corporation (wholly owned by affiliates of The Thompson Company) and subsidiaries (the Successor subsequent to the merger with JT Acquisition Corporation) as of December 31, 1987, and the related consolidated statements of operations, shareholders' equity and changes in financial position from August 1, 1987 (inception) to December 31, 1987; and the consolidated balance sheet of The Southland Corporation and subsidiaries (the Predecessor prior to the merger with JT Acquisition Corporation) as of December 31, 1986, and the related consolidated statements of operations, shareholders' equity and changes in financial position for the seven-month period ended July 31, 1987, and for the years ended December 31, 1986 and 1985, we have issued our report thereon dated March 23, 1988, which report is included herein. In connection therewith, we also examined the financial statement schedules of The Southland Corporation and Subsidiaries listed in Item 14.(a)2. herein. In our opinion, these schedules present fairly, when read in conjunction with the related consolidated financial statements, the financial data required to be set forth therein.

TOUCHE ROSS & CO.
Certified Public Accountants

Dallas, Texas
March 23, 1988

SCHEDULE V

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

PROPERTY, PLANT AND EQUIPMENT

Years ended December 31, 1985 and 1986, seven months ended July 31, 1987 and five months ended December 31, 1987 (Dollars in thousands)

	Land	Buildings and Leaseholds	Machinery and Equipment	Construction in Process	Total
Balance January 1, 1985	$317,768	$ 894,531	$682,713	$ 96,389	$1,991,401
Additions, at cost	75,288	151,303	123,629	52,038	402,258
Retirements or sales	(13,433)	(36,391)	(46,121)	—	(95,945)
Transfers to investment in properties	960	(18,916)	(21,152)	26,349	(12,759)
Balance January 1, 1986	380,583	990,527	739,069	174,776	2,284,955
Additions, at cost	98,916	194,827	223,947	159,073	676,763
Retirements or sales	(15,952)	(40,293)	(53,777)	—	(110,022)
Transfers to investment in properties	(7,295)	(1,890)	—	21,598	12,413
Balance January 1, 1987	456,252	1,143,171	909,239	355,447	2,864,109
Additions, at cost	70,845	124,936	123,742	77,248	396,771
Retirements or sales	(10,999)	(12,606)	(43,538)	—	(67,143)
Transfers to investment in properties	(400)	(600)	—	10,000	9,000
Balance July 31, 1987	515,698	1,254,901	989,443	442,695	3,202,737
Change due to revaluation for merger	35,728	(221,232)	(438,527)	(221,503)	(845,534)
Additions, at cost	149,334	114,545	7,828	(118,748)	152,959
Retirements or sales	(4,994)	(24,620)	(10,471)	—	(40,085)
Transfers to investment in properties	8,740	6,660	—	—	15,400
Balance December 31, 1987	$704,506	$1,130,254	$548,273	$102,444	$2,485,477

Depreciation of plant and equipment and amortization of capital leases is based upon the estimated useful lives of these assets using the straight-line method. Amortization of improvements to leased properties is based upon the remaining terms of the leases or the estimated useful lives of such improvements, whichever is shorter. Annual rates used in computing the provision for depreciation and amortization were as follows:

Buildings	2.5% to 14.3%
Furniture and fixtures	10% to 33.3%
Machinery and equipment	5% to 33.3%

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

ACCUMULATED DEPRECIATION AND AMORTIZATION OF PROPERTY, PLANT AND EQUIPMENT

Years ended December 31, 1985 and 1986
seven months ended July 31, 1987
and five months ended December 31, 1987
(Dollars in thousands)

	Buildings and Leaseholds	Machinery and Equipment	Total
Balance January 1, 1985	$328,481	$ 325,069	$653,550
Additions charged to expense	68,615	75,226	143,841
Retirements or sales	(12,204)	(36,082)	(48,286)
Balance January 1, 1986	384,892	364,213	749,105
Additions charged to expense	76,278	85,667	161,945
Retirements or sales	(25,180)	(41,632)	(66,812)
Balance January 1, 1987	435,990	408,248	844,238
Additions charged to expense	50,765	63,028	113,793
Retirements or sales	(9,366)	(35,277)	(44,643)
Balance July 31, 1987	477,389	435,999	913,388
Change due to revaluation for merger	(442,696)	(404,763)	(847,459)
Additions charged to expense	44,478	47,104	91,582
Retirements or sales	(9,391)	(7,092)	(16,483)
Balance December 31, 1987	$ 69,780	$ 71,248	$141,028

SCHEDULE IX

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

SHORT-TERM BORROWINGS

Five Months Ended December 31, 1987, Seven Months Ended July 31, 1987, and Years Ended December 31, 1986 and 1985
(Dollars in thousands)

Category of aggregate short-term borrowings(1)	Balance at end of period(2)	Weighted average interest rate	Maximum amount outstanding during the period(3)	Average amount outstanding during the period(4)	Weighted average interest rate during the period(5)
Five months ended December 31, 1987					
Commercial paper.......	$ —	—%	$ 63,817	$ 27,326	3.01%
Notes payable to banks..	—	—	184,543	109,643	3.47
Seven months ended July 31, 1987					
Commercial paper.......	$ —	—%	$193,606	$91,860	3.88%
Notes payable to banks..	224,725	6.98	224,725	117,892	3.90
Year ended December 31, 1986					
Commercial paper.......	$ 127,672	6.40%	$244,386	$ 62,994	7.18%
Notes payable to banks..	87,619	7.14	148,751	82,411	7.00
Year ended December 31, 1985					
Commercial paper.......	$ 275,030	8.31%	$275,030	$ 87,445	8.34%
Notes payable to banks..	21,590	7.71	90,399	39,191	8.57

(1) Commercial paper was issued throughout the year for periods ranging from one to 100 days, and notes payable were outstanding with maturities ranging from one to 91 days.

(2) Balance at end of period excludes notes payable classified as long-term debt in the amount of $27,000 at July 31, 1987, and commercial paper classified as long-term debt in the amounts of $173,000 at July 31, 1987, $200,000 at December 31, 1986 and $150,000 at December 31, 1985.

(3) Commercial paper amounts exclude $150,000 (except for $200,000 at the five months ended December 31, 1987, and the seven months ended July 31, 1987) classified as long-term debt. Notes payable amounts exclude $27,309 at the seven months ended July 31, 1987, classified as long-term debt.

(4) The average amount outstanding during the period was calculated by determining an average daily balance per month (excluding commercial paper classified as long-term debt), adding these average balances together, and dividing by the applicable number of months in the period.

(5) The weighted average interest rate during the period was calculated by dividing the average daily interest amount by the average daily principal balance.

SCHEDULE X

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

SUPPLEMENTARY INCOME STATEMENT INFORMATION

(Dollars in thousands)

	Successor	Predecessor		
	Five months ended December 31, 1987	Seven months ended July 31, 1987	Year ended December 31 1986	Year ended December 31 1985
Depreciation & Amortization of Intangibles	$38,420	$1,023	$ 1,410	$ 53

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors and Shareholders
CITGO Petroleum Corporation
Tulsa, Oklahoma

We have examined the consolidated balance sheets of CITGO Petroleum Corporation and subsidiaries as of December 31, 1987 and 1986, and the related statements of income, shareholders' equity and changes in financial position for each of the three years in the period ended December 31, 1987 and Schedules V,VI, VIII and X as required by Regulation S-X. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of CITGO Petroleum Corporation and subsidiaries as of December 31, 1987 and 1986, and the results of their operations and the changes in their financial position for each of the three years in the period ended December 31, 1987 in conformity with generally accepted accounting principles consistently applied during the period except for the change, with which we concur, in the method of valuing inventory of crude oil as described in Note 5 to the consolidated financial statements, and Schedules V,VI, VII and X present fairly, when read in conjunction with the related consolidated financial statements, the information therein set forth.

Touche Ross + Co.

Certified Public Accountants

Tulsa, Oklahoma
February 15, 1988

CITGO PETROLEUM CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)

ASSETS	December 31, 1987	1986
Current assets:		
Cash and cash equivalents	$ 1,392	$ 67,389
Accounts and notes receivable	243,985	228,326
Accounts receivable from related party	39,858	50,306
Inventories	413,750	412,217
Prepaid expenses	67,339	67,885
Total current assets	766,324	826,123
Property, plant and equipment-net	352,488	331,282
Investment in pipeline affiliates	46,776	46,925
Other assets	24,984	4,267
	$1,190,572	$1,208,597

LIABILITIES AND SHAREHOLDERS' EQUITY	1987	1986
Current liabilities:		
Accounts payable	$ 182,179	$ 154,301
Accounts payable to related party	54,027	78,254
Payroll and other taxes	40,560	15,571
Other current liabilities	77,473	56,895
Short-term borrowings	30,000	-
Income taxes	3,931	-
Long-term debt due within one year	2,170	2,170
Total current liabilities	390,340	307,191
Deferred income taxes	74,058	64,990
Other non-current liabilities	13,277	22,383
Long-term debt:		
Bank and other	276,133	263,303
Subordinated notes payable to shareholders	-	200,000
Total long-term debt	276,133	463,303
Minority interest in consolidated subsidiary	11,913	11,604
Shareholders' equity:		
Common stock-Class A, $1.00 par value, 1,000 shares authorized, issued and outstanding	1	1
Common stock-Class B, $1.00 par value, 1,000 shares authorized, issued and outstanding	1	1
Additional capital	274,979	274,979
Retained earnings	149,870	64,145
	424,851	339,126
	$1,190,572	$1,208,597

See notes to consolidated financial statements.

CITGO PETROLEUM CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME
(Dollars in Thousands)

	Years Ended December 31, 1987	1986	1985
Revenues:			
Outside sales	$2,880,235	$3,149,106	$4,108,039
Sales to related parties	1,057,593	953,515	1,581,539
	3,937,828	4,102,621	5,689,578
Other income	30,136	29,508	26,446
	3,967,964	4,132,129	5,716,024
Cost of sales and expenses:			
Cost of goods sold (including purchases of $836,026, $596,060, and $471,384 from related parties)	3,737,405	3,903,862	5,432,928
Inventory adjustment to market	-	84,751	74,800
Selling, general and administrative expenses	95,287	102,517	107,931
Interest expense:			
Related parties	11,508	16,851	15,827
Outside	16,430	14,154	22,671
Contributions to employees' savings plans	5,764	3,658	9,311
Minority interest in earnings of consolidated subsidiary	309	145	376
	3,866,703	4,125,938	5,663,844
Income before income taxes	101,261	6,191	52,180
Income taxes (credits)	15,536	(37,387)	12,889
Net income	$ 85,725	$ 43,578	$ 39,291

See notes to consolidated financial statements.

CITGO PETROLEUM CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION
(Dollars in Thousands)

	Years Ended December 31,		
	1987	1986	1985
Funds provided from operations:			
Net income	$ 85,725	$ 43,578	$ 39,291
Expenses not requiring the use of cash or cash equivalents:			
Depreciation and amortization	54,280	44,132	32,064
Deferred income taxes	8,812	23,668	(14,925)
Minority interest in earnings of consolidated subsidiary	309	145	376
	149,126	111,523	56,806
(Increase) decrease in accounts and notes receivable	(17,182)	138,108	(113,870)
Decrease (increase) in accounts receivable from related party	10,448	(52,376)	23,646
(Increase) decrease in inventories	(1,533)	231,257	61,983
Increase in prepaid expenses	(30,441)	(40,553)	(12,453)
(Increase) decrease in other assets	(20,717)	439	717
Increase (decrease) in accounts payable	27,878	(151,662)	(99,808)
(Decrease) increase in accounts payable to related parties	(24,227)	39,483	34,345
Increase (decrease) in payroll and other taxes	24,989	4,990	(8,896)
Increase (decrease) in other current liabilities	20,578	(6,973)	5,194
Increase (decrease) in income taxes	5,454	(32,022)	25,882
(Decrease) increase in other non-current liabilities	(9,106)	2,839	(9,479)
(Increase) decrease - other	(416)	1,108	6
Funds provided from (used in) operations	134,851	246,161	(35,927)
Investment activities:			
Property, plant and equipment additions	(46,699)	(30,555)	(11,129)
Property, plant and equipment retirements	3,021	3,059	3,257
Capital contribution	-	32,805	-
Sales of investments in affiliates	-	-	2,474
Funds (used in) provided from investment activities	(43,678)	5,309	(5,398)
Financing activities:			
Short-term borrowings	30,000	-	-
Long-term debt acquired:			
Bank and other	330,000	225,000	-
Shareholders	-	200,000	216,289
Long-term debt discharged:			
Bank and other	(317,170)	(72,170)	(182,170)
Shareholders	(200,000)	(355,914)	-
Repurchase of accounts receivable	-	(209,786)	(589)
Funds (used in) provided from financing activities	(157,170)	(212,870)	33,530
(Decrease) increase in cash and cash equivalents	$ (65,997)	$ 38,600	$ (7,795)

See notes to consolidated financial statements.

CITGO PETROLEUM CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(Dollars in Thousands)

	Years Ended December 31, 1987	1986	1985
Common stock:			
Balance, beginning of year	$ 2	$ 1	$ 1
Retirement	-	(1)	-
Issued - Class A	-	1	-
Issued - Class B	-	1	-
Balance, end of year	2	2	1
Additional capital:			
Balance, beginning of year	274,979	242,174	242,174
Capital contribution	-	32,805	-
Balance, end of year	274,979	274,979	242,174
Retained earnings:			
Balance, beginning of year	64,145	20,567	(18,724)
Net Income	85,725	43,578	39,291
Balance, end of year	149,870	64,145	20,567
Total shareholders' equity	$424,851	$339,126	$262,742

See notes to consolidated financial statements.

CITGO PETROLEUM CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 1987, 1986, AND 1985

1. ACCOUNTING POLICIES

Basis of Presentation

The consolidated financial statements include the accounts of CITGO Petroleum Corporation and its subsidiaries which include Cit-Con Oil Corporation (65% owned), CITGO Pipeline Company, CITGO International Supply Company, CITGO Caribbean Corporation, Foremost Petroleum Company of Texas, Inc. (Foremost), and minor subsidiaries (collectively referred to as the Company). All material intercompany transactions and accounts have been eliminated.

During 1985, Foremost and its subsidiaries and certain minor gasoline retail operations were wholly-owned subsidiaries or operations of The Southland Corporation (Southland). Effective January 1, 1986, Southland contributed the common stock of Foremost and the net assets of the other operations to the Company. The 1985 consolidated financial statements were prepared on the basis that the contributions were in effect at January 1, 1985.

The Company was acquired by Southland in 1983. The acquisition was accounted for as a purchase and, accordingly, the cost of the acquisition was recorded in the financial records of the Company.

The Company's investment in pipeline affiliates is accounted for by the equity method.

Revenues

The Company engages in crude oil trading to facilitate the receipt of crude oil at its refinery. Only the net results of such trading are recorded in cost of goods sold.

The Company also engages in refined products trading to facilitate the marketing of its refined products. The results of such trading are recorded in sales and cost of goods sold.

Other income is primarily comprised of equity in earnings of pipeline affiliates.

Inventories

Crude oil and refined product inventories are stated at the lower of cost or market. Cost is determined using the last-in, first-out (LIFO) method for refined products and, beginning in 1986, for crude oil. Prior to 1986, cost was determined using the first-in, first-out (FIFO) method for crude oil. The average cost method is used for materials and supplies.

Refinery Turnaround Maintenance

Costs of refinery turnaround maintenance are accounted for on the prepaid basis and are amortized over the average period between necessary turnarounds. Unamortized costs are included in prepaid expenses and other assets. Amortization of refinery turnaround costs is included in depreciation and amortization expense.

Depreciation

Depreciation of plant and equipment is based upon the estimated useful lives of the assets using the straight-line method.

Income Taxes

For the nine months ended September 30, 1986, Southland allocated income tax credits to the Company based on the income tax benefits generated by including tax losses of the Company in Southland's consolidated income tax provision for that period (Note 2). Prior to 1986, the Company was allocated income tax expense based on its pretax income using the consolidated effective tax rate of Southland.

Effective October 1, 1986, the Company began filing its own consolidated Federal income tax return. Cit-Con Oil Corporation files a separate Federal income tax return.

Deferred taxes are provided for and are a result of timing differences between financial and tax reporting.

2. SALE OF COMMON STOCK

As of September 30, 1986, Southland exchanged its existing shares of the Company's stock for 1,000 shares of Class A Common Stock, $1.00 par value and 1,000 shares of Class B Common Stock, $1.00 par value, and sold to Propercit, S.A. (a wholly-owned subsidiary of Petroleos de Venezuela, S.A. [PDVSA]) all of the Class A Common Stock. In 1987, Propercit, S.A. transferred the shares of Class A Common Stock to Propernyn B.V. (a wholly-owned subsidiary of PDVSA). Propercit, S.A. and PDVSA are corporations organized under the laws of the Republic of Venezuela. Propernyn B.V. is a corporation organized under the laws of the Netherlands. Both classes of common stock are vested with similar corresponding rights.

In connection with the transaction, the Company entered into a 20-year crude supply agreement with Commercit, S.A. (a wholly-owned subsidiary of Interven, S.A., which is wholly-owned by PDVSA) to purchase crude oil and feedstocks at market-related prices, and Southland entered into a 20-year product purchase agreement with the Company to buy refined products at market-related prices. In connection with the sale, Southland forgave certain intercompany indebtedness and contributed cash to the Company, which is included in additional capital.

3. RELATED PARTY TRANSACTIONS

During 1987 and 1986, the Company purchased approximately $836 million and $596 million of crude oil, feedstocks, and other products from Commercit, S.A. and affiliated companies. At December 31, 1987 and 1986, $54 million and $78.3 million are payable as a result of these transactions.

The Company had refined product sales to Southland of approximately $1,058 million in 1987, $954 million in 1986, and $1,549 million in 1985. The Company paid Southland approximately $4.8 million and $8 million during 1986 and 1985 for various legal, financial and other services provided to the Company. The Company established its own organization to perform these services in 1987. At December 31, 1987 and 1986, $39.9 million and $50.3 million are receivable as a result of these and other related transactions.

The Company is entitled to purchase, for a period not to exceed 15 years, certain crude oil produced in defined locations from Occidental Petroleum Corporation and its subsidiaries (Occidental), a shareholder of Southland during 1985. In 1985, the Company purchased $412.3 million of crude oil, at average posted prices, under this agreement. The Company is also entitled to purchase natural gas as fuel for its refinery from Occidental for a period not to exceed 20 years. During 1985, the Company purchased $37.1 million of natural gas under this agreement, and had purchases and sales of other feedstocks with Occidental amounting to $22 million and $32.8 million, respectively. At December 31, 1985, $38.8 million was payable to Occidental as a result of these transactions.

Prior to September 30, 1986, the Company repaid $355.9 million of notes payable due Southland under a previous loan arrangement. Interest expense on these notes was $13.5 million in 1986 and $15.8 million in 1985.

In connection with the common stock transaction (Note 2), the Company had available the borrowing capacity of $130 million in subordinated note agreements with each of Southland and PDVSA. The $200 million outstanding at December 31, 1986 was repaid during 1987 with proceeds from operations and the issuance of senior subordinated promissory notes (Note 9). Interest expense on these shareholder notes totaled $11.5 million in 1987 and $3.4 million in 1986.

The Company incurred refined product and crude oil transportation charges from pipeline affiliates of $48.7 million in 1987, $49.3 million in 1986, and $50.1 million in 1985.

4. ACCOUNTS AND NOTES RECEIVABLE

	(000's omitted) December 31, 1987	1986
Trade accounts and notes receivable	$249,405	$231,794
Income taxes receivable	-	1,523
	249,405	233,317
Less allowance for doubtful accounts	5,420	4,991
	$243,985	$228,326

On December 28, 1984, the Company sold $210 million of accounts receivable under an agreement in which the purchaser reinvested the proceeds from the collected receivables in new receivables for a period of five years. As of January 1, 1986, the Company had sold $209.8 million of accounts receivable under this agreement. The rollover of proceeds collected and reinvested in new accounts receivable aggregated $1.1 billion in 1986 and $3.9 billion in 1985. In connection with the common stock transaction, the Company ended this agreement and repurchased the outstanding receivables.

5. INVENTORIES

	(000's omitted) December 31, 1987	1986
Refined product	$298,949	$293,043
Crude oil	88,428	95,546
Materials and supplies	26,373	23,628
	$413,750	$412,217

The adjustment of refined product and crude oil inventories to market value, which is less than cost, was $176.3 million at December 31, 1987 and 1986, and $91.5 million at December 31, 1985.

The Company changed its method of accounting for crude oil inventory from the FIFO to LIFO method effective January 1, 1986. The change was made because management believes LIFO provides better matching of current costs with current revenue and minimizes the impact of price level changes on inventory valuations. The effect of this change in 1986 was to decrease cost of goods sold and increase the inventory adjustment to market value by $53.5 million, with no effect on net income. Included in the effect of this change was a charge of $12 million to cost of goods sold resulting from a liquidation of LIFO crude oil inventory quantities. The cumulative effect and pro forma results of operations for prior years, had LIFO been followed for crude oil inventory, is not determinable.

The reduction of refined product LIFO inventory quantities accumulated in prior years at higher costs resulted in increased cost of goods sold of $62.4 million in 1986.

There were no reductions of crude oil and refined product LIFO inventory quantities in 1987.

As a result of the acquisition of the Company by Southland, the historical tax basis for refined product inventories is less than the book LIFO basis (before adjustment to market value) by approximately $230 million at December 31, 1987 and 1986. The Company expects the levels of refined product inventories required for normal operations to exceed those acquired in 1983.

6. PROPERTY, PLANT AND EQUIPMENT

	(000's omitted) December 31, 1987	1986
Land	$ 27,127	$ 27,671
Buildings and leaseholds	75,518	72,848
Machinery and equipment	296,410	260,877
Vehicles	8,567	9,810
Construction in process	13,862	13,898
	421,484	385,104
Less accumulated depreciation and amortization	68,996	53,822
	$352,488	$331,282

Depreciation expense was $22.5 million in 1987, $23.6 million in 1986, and $23.4 million in 1985.

When the Company was acquired by Southland, generally accepted accounting principles required the allocation of the purchase price which reduced the historical book cost of property, plant and equipment. This reduction, net of amortization, was approximately $434 million and $457 million at December 31, 1987 and 1986.

7. INVESTMENT IN PIPELINE AFFILIATES

The Company's investment in pipeline affiliates is accounted for by the equity method and consists of equity interests of 6.8% to 50%. Equity in earnings of the affiliates is recorded net of amortization of the excess of purchase price over historical book value (straight-line over 40 years), which arose from the acquisition of the Company by Southland. Investment in pipeline affiliates exceeded the equity in the underlying net assets by $33 million and $34 million at December 31, 1987 and 1986. The summary financial information derived from data provided by these pipeline companies is as follows:

	(000's omitted) December 31, 1987	1986
Summary of financial position:		
Current assets	$ 102,629	$ 101,225
Noncurrent assets	1,117,033	1,151,140
Current liabilities	185,278	183,925
Noncurrent liabilities	943,994	979,977

	(000's omitted) Years Ended December 31, 1987	1986	1985
Summary of operating results:			
Revenues	$725,025	$742,543	$690,159
Gross profit	421,537	425,489	406,597
Net earnings	212,936	193,682	175,009
Company investment in pipeline affiliates	$46,776	$46,925	$ 48,032
Company equity in net earnings	26,627	23,673	22,603
Dividends received	26,776	24,780	22,609

8. SHORT-TERM BORROWINGS

In 1987, the Company entered into short-term borrowing facilities with various banks. The borrowing facilities are uncommitted and unsecured, and have maturities from 1 to 30 days. The interest rate on these facilities is based on Federal funds interest rates (weighted average effective rate of approximately 7.7% for 1987).

9. LONG-TERM DEBT

	(000's omitted) December 31, 1987	1986
Revolving loan - bank	$140,000	$225,000
Senior subordinated notes	100,000	-
Industrial development revenue bonds	29,200	29,200
Unsecured notes payable	9,103	11,273
Subordinated notes payable to shareholders (Note 3)	-	200,000
	278,303	465,473
Less amounts due in one year	2,170	2,170
	$276,133	$463,303

During 1987, the Company renegotiated its bank credit agreement (the Agreement) reducing its revolving line of credit from $500 million to $400 million while extending the term to a three-year revolving facility renewable on an annual basis for successive three-year periods. The Agreement provides for several borrowing maturities and interest rate options (weighted average effective rate of approximately 7.6% for 1987). Borrowings under the Agreement are collateralized by crude oil and refined product inventories and certain accounts receivable, which have book values of approximately $596 million at December 31, 1987. The Agreement contractually extends through August 26, 1990, with options for automatic renewal as long as a commitment of $400 million is maintained from acceptable banks. It is the intent of Company management that these borrowings will be renewed, or replaced with other long-term credit facilities. The Agreement contains certain covenants that place limitations on the Company for incurring additional debt, placing liens on property, and selling and acquiring fixed assets. The Company was in compliance with the debt covenants at December 31, 1987.

In December 1987, the Company issued $100 million of senior subordinated promissory notes (the Notes). The Notes consist of $60 million of Series A Notes, bearing interest at 10.60% per year payable semiannually, with annual principal installments of $15 million beginning December 1, 1989; and $40 million of Series B Notes, bearing interest at 10.90% per year payable semiannually, with annual principal installments of $8 million beginning December 1, 1990. The Notes are subordinate to the bank credit agreement and other senior indebtedness of the Company. The Notes restrict the Company to paying dividends based on consolidated net income (as defined in the Notes). The Notes contain certain other covenants that place limitations on the Company for placing liens on property, acquiring additional debt and selling and acquiring fixed assets. The Company was in compliance with the Note covenants at December 31, 1987.

Industrial development revenue bonds aggregating $17.4 million are due in 2004, with the remaining $11.8 million due in 2007. Interest is payable monthly based on floating market interest rates (weighted average effective rate of approximately 4.8% for 1987).

The unsecured notes payable consist of $8.7 million bearing interest at the prime rate. These notes are payable in equal annual installments through 1991, with interest payable quarterly. In addition, a $.4 million unsecured note is due in 1992 with interest at 10%.

As of December 31, 1987, long-term debt scheduled maturities are: 1988 - $2.2 million, 1989 - $17.2 million, 1990 - $165.1 million, 1991 - $25.2 million, 1992 - $23.4 million and $45.2 million thereafter.

10. EMPLOYEE BENEFIT PLANS

Stock Options

The Company's Phantom Stock Option Plan (the Option Plan) provided participants with the right to exercise options for cash equal to the difference between the option price and the market value of Southland common stock at exercise date. The Option Plan included a provision that all outstanding options became exercisable if substantially all of the stock of Southland were acquired by another party. In connection with the 1987 acquisition of Southland by J. T. Acquisition Corporation, all options became exercisable which resulted in $8 million of expense in 1987. The Option Plan has been terminated.

Employee Savings

Salaried employees of the Company were eligible to participate in The Southland Corporation Employees' Savings and Profit Sharing Plan (Profit Sharing) through 1986. Contributions to Profit Sharing were made by the participants and the Company. Southland charged the Company $3.7 million in 1986 and $9.3 million in 1985 for Profit Sharing contributions which was approximately equal to the benefits credited to Company participants.

Effective January 1, 1987, the Company terminated participation in Profit Sharing and established the Employees' Retirement and Savings Plan (RASP) for its eligible salaried employees. Contributions to RASP are made by participants and the Company. The Company contributions to RASP are based on participants' pretax contributions and years of service. The Company expensed $5.8 million for matching funds during 1987.

Benefits

The Company has a thrift plan for the majority of its hourly employees. Contributions to the thrift plan are subject to sufficient accumulated taxable earnings and profits and are based on employee contributions and years of service. The Company expensed $1 million in 1987 and $.9 million in 1986 and in 1985 for its thrift plan.

The Company also has a non-contributory, defined benefit pension plan (the Pension Plan) for the majority of its hourly employees. The Pension Plan pays benefits to participants at retirement using formulas based upon years of service and compensation levels as specified. The Pension Plan assets consist primarily of bonds, common stock and temporary cash investments. The Company's funding policy is to fund an amount, as determined by the Company and its independent actuary, that will meet the minimum funding required by applicable law and maximize the tax benefit to the Company. Effective January 1, 1987, the Company adopted Statement of Financial Accounting Standards No. 87, Employers' Accounting for Pensions, which did not have a material effect on 1987 net income.

The discount rate used in determining the actuarial present value of accumulated benefits in 1987 was 7.5%. The expected long-term rate of return on assets was 7.5%. Although the annual rates may vary, the rate of the long-term compensation increase was assumed to be 6%. The pension expense calculation is as follows:

	(000's omitted) 1987
Service cost (benefits earned during the year)	$ 3,224
Interest cost on projected benefit obligation	3,844
Actual return on plan assets	(4,465)
Net amortization and deferred items	732
Net pension expense	$ 3,335

Pension expense was $2.7 million in 1986 and $2.2 million in 1985.

The following table shows the funded status of the Pension Plan and the amount reported in the Company's consolidated financial statements:

	(000's omitted) December 31, 1987	
Pension Plan assets at fair value		$ 55,016
Actuarial present value of benefit obligations:		
Vested benefits	$(30,489)	
Nonvested benefits	(2,173)	
Accumulated benefit obligation	(32,662)	
Effect of projected long-term compensation increases	(12,122)	
Total projected benefit obligation		(44,784)
Pension Plan assets in excess of projected benefit obligation		10,232
Unrecognized net gain at adoption		(224)
Unrecognized net gain due primarily to change in discount rate to 9%		(13,343)
Accrued pension liability		$ (3,335)

Postretirement Insurance Benefits

Under a plan that covers both active and retired employees, the Company provides certain health care and life insurance benefits for retirees through a trust that is funded partially by the participants and the balance by the Company. Substantially all employees may become eligible for these benefits if they reach the normal retirement age or qualify for early retirement. In the opinion of Company management, the Company has the right to discontinue these benefits at its discretion. The cost of retiree health care and life insurance benefits is expensed and funded as claims are paid and for 1987 was $1.4 million, 1986 was $1.1 million, and 1985 was $.7 million.

11. INCOME TAXES

The provisions for income taxes (credits) are as follows:

	1987	1986	1985
		(000's omitted)	
Current tax expense (credits):			
Federal	$ 6,403	$(59,892)	$ 35,334
State	321	(1,163)	(7,520)
Deferred tax expense	8,812	23,668	(14,925)
Total income tax expense (credits)	$15,536	$(37,387)	$ 12,889

Deferred tax expense results from timing differences in the recognition of revenue and expense for tax and financial accounting purposes. The sources of these differences and the net tax effect of each are as follows:

	1987	1986	1985
		(000's omitted)	
Accelerated depreciation	$4,023	$ 7,424	$ 25,037
Inventory adjustments	2,360	8,241	(34,710)
Refinery turnaround expenditures	3,238	4,772	1,990
Bad debt expense	(643)	(700)	(1,720)
Insurance claim settlements	-	-	(1,242)
Employee benefit trust contributions	-	(55)	(1,683)
Accrual deducted for tax purposes	(156)	4,172	-
Other, net	(10)	(186)	(2,597)
Total deferred tax expense (credits)	$8,812	$23,668	$(14,925)

Deferred Federal income taxes at December 31, 1987 and 1986, are $74.1 million and $65 million. Net deferred Federal income tax benefits of $32.8 million and $32.5 million at December 31, 1987 and 1986, are included in prepaid expenses.

The provisions for income taxes (credits) vary from the statutory rate as follows:

	1987	1986	1985
		(000's omitted)	
Federal statutory tax	$ 40,504	$ 2,848	$ 24,002
(Decreases) increases resulting from:			
Amortization of excess tax basis over book basis (Note 6)	(17,816)	(30,512)	(38,133)
Dividend exclusion	(8,336)	(9,300)	(8,982)
State income tax	193	(628)	(4,061)
Southland effective tax rate adjustment (Note 1)	-	-	40,063
Other	991	205	-
	$ 15,536	$(37,387)	$ 12,889

At December 31, 1987, the Company has approximately $30.6 million of net operating loss carryforwards for tax purposes of which $13.6 million expires in 2001 and $17 million in 2002.

The Company's Federal alternative minimum tax was $5.7 million for 1987 which can be used to offset regular Federal income taxes in future years subject to alternative minimum tax limitations.

12. COMMITMENTS AND CONTINGENCIES

Certain obligations of pipeline affiliates are secured by long-term cash support agreements of the Company and other owner companies. Cash support provided is recouped in following years. The Company has not been required to provide cash support in connection with these agreements since 1979 and this support was fully recouped in 1980.

The Company has various noncancellable operating leases, primarily for office space, machinery and equipment, and vehicles. Future minimum lease payments for these leases with remaining noncancellable terms in excess of one year are as follows: 1988 - $10.2 million; 1989 - $9 million; 1990 - $8.2 million; 1991 - $7 million; 1992 - $5.7 million; and $5.4 million thereafter. Rent expense on all operating leases totaled approximately $13 million for 1987 and $11 million for 1986 and for 1985.

On January 26, 1988, the Board of Directors declared a dividend of $25 million, payable to the holders of the Class A Common Stock and Class B Common Stock of record as of the close of business on January 26, 1988. The dividend is payable on February 29, 1988.

The Company is subject to Federal and state laws and regulations related to the protection of the environment, including specifically, the use, storage and disposal of hazardous materials. The Company believes that protection and preservation of the environment is of the highest priority and importance. Management believes the Company is currently in substantial compliance with these laws and regulations. These laws and regulations are subject to revision and reinterpretation, and maintaining compliance with them in the future could possibly necessitate significant capital expenditures.

Various suits and claims arising in the ordinary course of business are pending against the Company. While the ultimate effect of such actions cannot be ascertained at this time, in the opinion of General Counsel of the Company, resolution of such actions should not result in a material effect on the financial position of the Company.

Schedule V

CITGO PETROLEUM CORPORATION AND SUBSIDIARIES

PROPERTY, PLANT AND EQUIPMENT

Years Ended December 31, 1987, 1986 and 1985
(Dollars in Thousands)

	Land	Buildings and Leaseholds	Machinery and Equipment	Vehicles	Construction in Process	Total
Balance December 31, 1984...........	$28,085	$19,474	$305,305	$ 7,411	$ 9,870	$370,145
Additions at cost...................	272	2,087	8,706	406	(342)	11,129
Retirements or sales................	(922)	(1,143)	(9,251)	(1,158)	-	(12,474)
Reclassifications...................	-	37,426	(37,364)	(62)	-	-
Balance December 31, 1985...........	27,435	57,844	267,396	6,597	9,528	368,800
Additions at cost...................	-	2,586	14,488	3,238	10,243	30,555
Retirements or sales................	(1)	(1,141)	(11,974)	(1,135)	-	(14,251)
Transfers and reclassifications.....	237	13,559	(9,033)	1,110	(5,873)	-
Balance December 31, 1986...........	27,671	72,848	260,877	9,810	13,898	385,104
Additions at cost...................	49	2,587	39,480	329	4,254	46,699
Retirements or sales................	(593)	(1,056)	(2,946)	(5,724)	-	(10,319)
Transfers and reclassifications.....	-	1,139	(1,001)	4,152	(4,290)	-
Balance December 31, 1987...........	$27,127	$75,518	$296,410	$ 8,567	$13,862	$421,484

Depreciation of plant and equipment is based upon the estimated useful lives of these assets using the straight-line method. Annual rates used in computing the provision for depreciation and amortization were as follows:

Buildings...................................	4.2% to 10%
Leasehold improvements......................	Term of lease
Machinery and equipment.....................	4.2% to 33.3%
Vehicles....................................	7.4% to 33.3%

Schedule VI

CITCO PETROLEUM CORPORATION AND SUBSIDIARIES

ACCUMULATED DEPRECIATION AND AMORTIZATION OF PROPERTY, PLANT AND EQUIPMENT

Years ended December 31, 1987, 1986 and 1985
(Dollars in Thousands)

	Buildings and Leaseholds	Machinery and Equipment	Vehicles	Total
Balance December 31, 1984..........	$ 3,124	$ 21,670	$ 2,394	$ 27,188
Additions charged to expense.......	4,659	17,385	1,385	23,429
Retirements or sales...............	(544)	(7,969)	(704)	(9,217)
Balance December 31, 1985..........	7,239	31,086	3,075	41,400
Additions charged to expense.......	5,279	17,161	1,174	23,614
Retirements or sales...............	(1,055)	(9,221)	(916)	(11,192)
Transfers and reclassifications....	18,774	(19,003)	229	-
Balance December 31, 1986..........	30,237	20,023	3,562	53,822
Additions charged to expense.......	6,171	15,131	1,170	22,472
Retirements or sales...............	(891)	(2,412)	(3,995)	(7,298)
Transfers and reclassifications....	854	(901)	47	-
Balance December 31, 1987..........	$36,371	$ 31,841	$ 784	$ 68,996

CITGO PETROLEUM CORPORATION AND SUBSIDIARIES

VALUATION AND QUALIFYING ACCOUNTS

Years Ended December 31, 1987, 1986 and 1985
(Dollars in Thousands)

Allowance for Doubtful Accounts and Notes Receivable

Balance December 31, 1984	$ 4,604
Additions charged to expense	5,807
Deductions credited to receivable	(3,260)
Balance December 31, 1985	7,151
Additions charged to expense	4,052
Deductions credited to receivable	(6,212)
Balance December 31, 1986	4,991
Additions charged to expense	14,670
Deductions credited to receivable	(14,241)
Balance December 31, 1987	$ 5,420

Lower of Cost or Market Adjustment - Inventories

Balance December 31, 1984	$ 16,717
Additions charged to expense	74,800
Balance December 31, 1985	91,517
Additions charged to expense	84,751
Balance December 31, 1986	176,268
Additions charged to expense	-
Balance December 31, 1987	$176,268

CITGO PETROLEUM CORPORATION AND SUBSIDIARIES

SUPPLEMENTARY INCOME STATEMENT INFORMATION
(Dollars in Thousands)

	Years Ended December 31,		
	1987	1986	1985
Maintenance and repairs	$65,833	$65,835	$53,532

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Dallas, State of Texas, on the 28th day of March 1988.

THE SOUTHLAND CORPORATION

/s/ JOHN P. THOMPSON

John P. Thompson
Chairman of the Board

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this report has been signed by the following persons on behalf of the registrant and in the capacities indicated and on the date indicated.

Signature	Title	Date
/s/ JOHN P. THOMPSON John P. Thompson	Chairman of the Board	March 28, 1988
/s/ JERE W. THOMPSON Jere W. Thompson	President and Chief Executive Officer and Director (Principal Executive Officer)	
/s/ CLARK J. MATTHEWS, II Clark J. Matthews, II	Executive Vice President and Chief Financial Officer (Principal Financial Officer)	
/s/ VERNON P. LOTMAN Vernon P. Lotman	Controller (Principal Accounting Officer)	
/s/ JOE C. THOMPSON, JR. Joe C. Thompson, Jr.	Director	

7-Eleven: The Premier Convenience Retailer

As one of the world's best-known and most innovative retailers, 7-Eleven relies on its store managers, franchisees and their staffs to provide the best value and customer service in convenience retailing.

The Southland Corporation P.O. Box 719, Dallas, Texas 75221